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**Working Paper**

## Trends and Phases in the Colombian Economy and Its Foreign Trade and Payments, 1950-70

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CENTER DISCUSSION PAPER NO. 139

TRENDS AND PHASES IN THE COLOMBIAN ECONOMY AND  
ITS FOREIGN TRADE AND PAYMENTS, 1950-1970\*

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## Chapter I

### Trends and Phases in the Colombian Economy and its Foreign Trade and Payments, 1950-1970\*

This chapter will review major trends in Colombian foreign trade and payments from (about) 1950 to 1970. Contemporary developments in the rest of the economy will also be discussed, but more selectively; breaking a sector away and analyzing it separately 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 hopefully help yield richer fruit.

This chapter will also contribute a first subdivision of 1950 to 1970 into periods characterized by different external circumstances, as well as by varied domestic policy responses.

#### An Overall View: Gross Domestic Product

The post war growth of the Colombian economy has been far from spectacular; as shown in Table I-1, which also presents growth rates for other macro-economic variables, real gross domestic product (GDP) expanded at an average annual rate of 4.6 percent during 1950 through 1969. Between those years population grew at 3.2 percent per annum. Per capita GDP towards the end of the period under study remained at a level about average for Latin America, or roughly \$350. This is, incidentally, only one of the ways in which Colombia appears to be the country closest to being a "typical" Latin American nation.

Primary production, including rural activities and fishing, as well as mining, accounted in 1969 for 30 percent of GDP (at current prices); the corresponding amount was 38 percent in 1950. The real output of this sector as a whole grew at a rate not significantly different from that of population.

Table I-1

Average Annual Growth Rates of Key Variables in the Colombian Economy

(and their Standard Errors)

(Percentages)

	1948 through 1970 <sup>w</sup>	1948 through 1956 <sup>x</sup>	1957 through 1970 <sup>y</sup>	1956 through 1967
1. Merchandise exports, current dollars	1.60 (0.55)	9.94 (1.48)	2.18 (0.54)	0.03 (0.83)
2. Coffee exports, current dollars	0.34 (0.69)	10.88 (1.71)	0.47 (0.77)	-2.05 (0.89)
3. Dollar price of coffee	-0.65 (0.69)	9.51 (1.81)	-0.69 (0.89)	-3.35 (1.24)
4. Quantum of coffee exports	1.06 (0.29)	1.13 (1.60)	1.30 (0.49)	1.43 (0.70)
5. Merchandise imports, current dollars	2.46 (0.65)	11.58 (1.64)	3.41 (0.82)	0.85 (1.40)
6. Quantum of merchandise imports	0.74 (0.71)	10.49 (1.54)	1.19 (0.88)	-0.86 (1.39)
7. Real gross domestic product, at factor cost	4.59 (0.06)	5.23 (0.22)	4.79 (0.07)	4.57 (0.09)
--a) Primary production	3.29 (0.06)	2.86 (0.21)	3.19 (0.13)	3.06 (0.12)
--b) Manufacturing	6.03 (0.09)	7.25 (0.33)	5.65 (0.09)	5.68 (0.10)
--c) Construction	5.41 (0.53)	12.85 (1.88)	5.25 (0.81)	3.21 (0.75)
--d) Services: Type I	5.24 (0.19)	7.43 (0.68)	5.97 (0.17)	5.64 (0.33)
--e) Services: Type II	4.85 (0.07)	4.26 (0.14)	5.30 (0.05)	5.22 (0.10)

Table I-1 (continued)

	1948 through 1970 <sup>w</sup>	1948 through 1956 <sup>x</sup>	1957 through 1970 <sup>y</sup>	1956 through 1967
8. Domestic real fixed capital formation	3.01 (0.57)	11.41 (1.97)	4.45 (0.50)	2.64 (0.90)
--a) Capital goods import quantum (I)	-0.13 (1.02)	13.32 (2.89)	2.90 (1.14)	0.60 (1.93)
--b) Industrial production of capital goods	14.32 (0.66)	17.25 (1.31)	10.92 (0.99)	12.88 (0.98)
--c) Construction and building	4.60 (0.41)	9.44 (1.89)	4.61 (0.65)	2.99 (0.57)
--d) All investment in machinery and equipment	1.41 (0.91)	13.10 (2.67)	4.27 (0.99)	2.40 (1.72)

<sup>w</sup>Growth rates for items under (7) and (8) refer to 1950 through 1969 only; that for line (6) refers to 1948 through 1969 only.

<sup>x</sup>Growth rates for items under (7) and (8) refer to 1950 through 1956 only.

<sup>y</sup>Growth rates for items under (6), (7) and (8) refer to 1957 through 1969 only.

Sources and method: Growth rates were estimated by fitting the following regression to the basic data:

$$\log X_t = a + b t$$

where  $X_t$  refers to the relevant variable, and  $t$  to a time trend. The coefficient  $b$  will yield the growth rate; its standard error will provide a measure of instability.

Basic data obtained from International Financial Statistics (IMF), several issues, and Banco de la República, Cuentas Nacionales. "Primary production" includes agriculture, livestock, fishing and hunting, forestry and mining. "Services: Type I" include commerce, transport, communications, electricity, gas and water, and banking and insurance. "Services: Type II" include housing services, government and personal services.

In spite of massive rural-urban migrations, by 1970 about 59 percent of the total population still lived outside the 30 principal urban conglomerations, all having at least 50,000 inhabitants. These 30 urban centers grew during the period under study at the remarkable annual rate of 6.5 percent. Of the economically active population, it has been estimated that 43 percent could be regarded as rural.

Value added by the rural coffee sector by itself amounted to 8 percent of GDP in 1950, at current prices; by 1969 that percentage had declined to an estimated 4 percent. Were Colombian output to be measured at "world prices", those percentages would undoubtedly be higher, inter alia because coffee output is valued at (post-tax) prices received by producers. Coffee output has expanded at an annual rate of 1.6 percent, not far ahead of the growth of the coffee export quantum (1.1 percent per annum). In other words, the performance of the non-coffee primary sector is significantly superior to that suggested by Table 1.

Measured at current prices, the manufacturing share of GDP in 1969 is about what it was in 1950, around 18 percent, although manufacturing annual growth, measured in real terms, was 1.3 times that of GDP between those two years. Manufacturing employment, however, appears to have expanded at a rate similar to that of overall population, and thus lower than the growth in city-dwellers.

Construction and those services more closely linked to commodity production and distribution (Type I in Table I-1) saw their GDP share expand from 25 percent in 1950 to nearly 33 percent in 1969. Such upward trend has been stimulated by the urbanization and modernization undergone by Colombia between those years, and probably absorbed a large share of the

increments to the urban labor force. But these services grew less than manufacturing. Type II-services, closer to pure "home goods", kept their share of about 19 percent of GDP between 1950 and 1969, growing only slightly faster than GDP.

#### An Overall View: Foreign Trade

The volume of Colombian merchandise imports showed no clear upward trend, as indicated in Table I-1, when the period 1948 through 1969 is taken as a whole. Even at current dollar values, imports and exports show annual growth rates far below those of real GDP, manufacturing, and even primary production. No leading sector can be detected here; indeed, many authors have identified the sluggish expansion of Colombia's post war capacity to import as the major brake on growth.<sup>1</sup>

Coffee amounted to 78 percent of all merchandise exports in 1948, and the value of coffee exports, which as a first approximation can be said to be determined exogenously from Colombia's viewpoint, showed no significant upward trend for 1948-70 taken as a whole. Perhaps little more need be said to define Colombia's post war foreign trade plight. It may be added that the major non-coffee export in 1948 was crude oil, with 16 percent of exports; the expansion of this item could be said to have something to do with domestic policy, but much more with luck. Under the assumption of constant coffee and oil exports, even a 10 percent annual growth in non-coffee, non-oil ("minor") exports during 1948-70 would yield a 1.6 percent annual expansion in all exports. A 15 percent yearly growth of minor exports would still result in an overall export expansion of 3.7 percent per annum. In fact, comparing 1948-49-50 with 1968-69-70, one obtains an average annual growth rate for coffee plus oil exports (in current dollars) of 1.7 percent, and of 11.9 percent

for "minor" exports. The corresponding rate for all exports is 3.2 percent (note the difference which the calculation method makes). Put another way, coffee plus oil, which during 1948-49-50 represented 94 percent of the export bill, contributed only 41 percent of the expansion in export earnings between those years and 1968-69-70, by which period minor exports accounted for 31 percent of all exports.

#### External and Internal Instability

Colombia has been one of the classic examples of the export economy which relies on a major staple whose price is subject to considerable fluctuations in world markets. But even during the early nineteen fifties, exports of goods and services did not exceed 16 percent of GDP (at current prices), and in 1950 that percentage was only 11. The corresponding figure for 1969 was 13 percent. (It will be seen later that substantial fluctuations took place during the period under study in the price of tradeable goods relative to those of non-tradeables).

The first column of Table I-1 shows that two pieces of "conventional wisdom" regarding the typical Latin American export economy hold up reasonably well for the Colombia of 1948 through 1970. 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 5 and 6; never mind here quality complications). The coffee dollar price registered considerable instability, as measured by the standard error of the estimated annual rate of change; contrary to what has been argued for other countries,<sup>2</sup> the expansion of the coffee export quantum shows a much smaller standard error. The substantial fluctuations registered in the growth of dollar earnings of coffee exports can then be properly blamed mostly on price fluctuations.



Indeed, for 1948 through 1970, the correlation between (the logarithm of) the dollar value of coffee exports and (the logarithm of) the dollar price index of coffee yields an  $R^2$  of 0.77; a similar correlation between coffee export value and coffee export quantum yields an  $R^2$  of 0.02. Instability in coffee export earnings was decreased in some years by a negative correlation between price and quantity performance, but for the whole period that correlation was weak, as reflected by a negative  $R$  of only 0.33 between the logarithms of price and quantity. If the (significant) upward trend in the coffee export quantum is taken into account, the negative price-quantity link is further weakened for the period as a whole.

Less recognized is the fact that import instability during 1948 through 1970 was higher than export instability,<sup>3</sup> whether measured with respect to dollar value or in volume. Clearly such instability cannot be blamed solely on external circumstances, and the role of domestic policies will play a prominent place in the explanation of this peculiar fact. More on this in later chapters.

To one accustomed to the literature stressing the dependence of the Colombian domestic economy on foreign trade, and after confirming the unstable nature of imports and exports, it is surprising to find that the standard error corresponding to GDP growth is so small in the first column of Table I-1. Had one used a macroeconomic measure embodying terms of trade effects (which the GDP does not), the instability would of course be higher, but it is nevertheless notable that the fluctuations in exports and imports appear to find small echoes in GDP expansion. Even more striking, in view of much literature stressing rigid links, is the steadiness

found in manufacturing growth for the whole period. Which is the most unstable component of GDP? Construction, which presumably is one of the least import- (or export-) intensive sectors of the economy!<sup>4</sup>

The trade, especially import, fluctuations are so much larger than those of GDP that one could argue, attempting to reverse 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.

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 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 through 1968, and for 1929 through 1968.<sup>5</sup>

For any given year it appears that above a certain minimum, (in fact available to Colombia during almost all 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 non-durable consumer goods, can of course be postponed without much loss of that year's GDP. Intermediate and raw material inputs, spare parts, etc., are a more difficult matter, but an on-going economic system,

especially one accustomed to import controls (and even one without such habits, as Cuba from 1959 on) can in the short run partly absorb fluctuations in import availability via changes in inventories as well as using more imaginative expedients, decreasing (but not eliminating) their negative impact 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; together with many services and even parts of manufacturing (especially craft) a robust sector of non-tradeables can be put together, the hard core of it being found geographically among the small cities and towns scattered amidst the abrupt Colombian mountains.

The above considerations help to explain why the link between foreign trade and GDP growth in Colombia has been a relatively weak one, when looking basically at year-to-year changes. It has less to say regarding longer term links.

#### Capital Formation and Foreign Trade

Real fixed capital formation in Colombia grew during 1950 through 1969 at a lower rate than GDP, as can be seen in line (8) of Table I-1. Domestic production of capital goods, starting from a low base, expanded at a rapid clip, while construction grew at a rate similar to GDP. The volume of capital good imports, however, stagnated when 1950-70 is looked at as a whole.<sup>6</sup> In other words, there was no significant difference in the growth performance of the overall import quantum and that corresponding to capital goods. As imports accounted for more than 90 percent of capital formation in the form of machinery and equipment in 1950, and still accounted

for about 75 percent of that investment in 1969, the failure of import capacity to rise over the long run seriously limited investment and probably important aspects of technical change. Capital formation in machinery and equipment taken as a whole shows a 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 capital good imports are the highest. Here is where trade instability (and stagnation) take their sharpest bite. As it will be seen in later chapters, 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 during the studied period. Under these circumstances, the export sector is the major (indirect) supplier of machinery and equipment.<sup>7</sup>

Not surprisingly, in view of the link between foreign trade and capital formation, the relative prices of capital goods in Colombia, especially machinery and equipment, have on the whole followed the acute gyrations of the prices for tradeable goods relative to non-tradeables. So while the share of gross fixed investment in GDP, when measured at current prices was 14 percent in 1950 and 19 percent in 1969, the corresponding figures, when series at constant 1958 prices are used, are 19 percent for 1950 and 17 percent for 1969.

#### Coffee and Phases

Clearly the period 1948 through 1970 covers a variety of trade and domestic experiences, which deserve separate treatment. The basic nature

of the Colombian economic system remained, of course, unchanged, but dollar coffee prices as well as exchange and import policies differed substantially from period to period.

A first subdivision, based on the coffee market, is easy to make: before and after 1956. As shown in Table I-1, coffee prices showed an impressive upward trend from 1948 through 1956, dragging upwards export and import dollar values, as well as the import quantum and fixed capital formation. GDP rose from 1950 through 1956 at a faster than average (for 1950-69) 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 sectorial 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. A good part of rural Colombia was during 1948-1956 in the midst of social turmoil and/or bloody civil war. Another name for growth and development, or for favorable terms of trade, is not always peace, as this experience shows.

The years from 1957 through 1970 witnessed, on the whole, less favorable conditions in world coffee markets than 1948-1956. The coffee trends were particularly depressing through 1967, as shown in Table I-1. Colombian attempts to cope with such a situation will make up much of the substance of later chapters.

While the annual growth in the import quantum dropped from 10.5 to 1.2 percent, GDP growth sagged by only less than half a percentage point, from 5.2 to 4.8. The slowdown in manufacturing expansion was larger, from 7.3 to 5.7 percent per year, although far less dramatic than the drop

in the construction (value added) growth rate, which went from 12.9 to 5.3 percent per annum. These contrasts are accentuated if the years 1948-1956 are compared with 1956 through 1967; this latter period witnessed a falling trend in the import quantum, in spite of which GDP and manufacturing grew at respectable rates, not so far from those of 1948 through 1956. Non-tradeable construction services, paradoxically, grew only like population during 1956 through 1967.

Capital formation, especially in machinery and equipment, behaves more like the trade variables than like GDP and manufacturing (not to mention the steadier, in spite of weather, primary production), when comparing pre- with post-1956 trends. The slowdown in the expansion of domestic production of capital goods is notable, but that growth remained at an impressive level, especially taking into account the larger post-1956 base.

The Colombian social and political picture, one may add, was quieter and more peaceful during 1957 through 1970 than during the earlier phase.

#### Policy and Subphases: Before the Fall

While trends in coffee prices provide the critical 1956 watershed in Colombian post war economic history, no such simple, single criterion can be found to further subdivide the two major phases. Annex B provides a list of principal post war 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; 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.

Subdivisions of the pre- and post-1956 phases will naturally be somewhat arbitrary, but it is hoped that those suggested in Table I-2 will add, on balance, more light than confusion. The last three follow, as well as calendar years allow, the post-1958 terms of the National Front Presidents. They are preceded by two biannual transitional subphases (1957-58 and 1955-56), and by 1950 through 1954. Brief sketches of the characteristics of each of these subphases at this point may place later discussion in perspective.

As in many Latin American countries, the great depression of the nineteen thirties put an end to an era of relative economic liberalism in Colombia. Widespread exchange and import controls were introduced in 1931; they have not been fully abandoned ever 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) for the real exchange rate, adjusted for price level changes both in Colombia and the U.S., went from 56 in 1929 to 101 in 1935, when GDP deflators are used as proxies for "the price level", or from 70 in 1929 to 103 in 1935, when cost of living indices are employed.<sup>8</sup> 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 until 1958.

Table I-2

Major Colombian Economic Indicators, including Some Policy Variables

(Annual Averages)

	1950 through <u>1954</u>	1955 and <u>1956</u>	1957 and <u>1958</u>	1959 through <u>1962</u>	1963 through <u>1966</u>	1967 through <u>1970</u>
<u>Foreign trade indices (averages for</u> the whole period equal 100)						
--Merchandise exports (current dollars)	99	112	93	88	97	115
--Coffee plus oil exports (current dollars)	109	122	98	90	94	95
--Other (minor) exports (current dollars)	35	58	59	72	118	234
--Dollar price of coffee	117	131	111	83	87	88
--Quantum of coffee exports	92	94	88	106	103	111
--Merchandise imports (current dollars)	88	121	90	92	101	122
--Quantum of merchandise imports						
<u>GDP and components average annual</u> growth rates (percentages)						
--GDP	5.6	4.0	2.3	5.5	4.6	5.6 <sup>x</sup>
--Primary production	2.9	3.2	4.5	3.1	2.7	5.1 <sup>x</sup>
--Manufacturing	7.1	7.0	4.5	6.8	5.5	5.7 <sup>x</sup>
--Construction	13.6	5.5	4.2	6.2	2.3	13.4 <sup>x</sup>
--Services: Type I	9.1	2.4	2.3	8.2	5.9	5.4 <sup>x</sup>
--Services: Type II	4.1	5.0	3.8	5.2	5.7	5.0 <sup>x</sup>
<u>Fixed capital formation as a percentage</u> of GDP (at 1958 prices)						
--In building and construction	20.1	23.9	16.5	18.2	16.2	16.9 <sup>x</sup>
--In machinery and equipment	8.8	10.4	9.7	9.8	8.5	10.1 <sup>x</sup>
--Overall marginal capital-output ratio,	11.3	13.5	6.8	8.4	7.7	6.8 <sup>x</sup>
one year lag	3.4	6.1	8.6	3.2	3.6	3.0 <sup>x</sup>



Table I-2 (continued)

	1950 through <u>1954</u>	1955 and <u>1956</u>	1957 and <u>1958</u>	1959 through <u>1962</u>	1963 through <u>1966</u>	1967 through <u>1970</u>
<u>Real exchange rates, 1958 prices</u> (Pesos per Dollar)						
--De facto coffee rate	4.2	4.5	5.3	5.2	4.7	5.0
--Average import rate	6.1	5.7	8.7	8.9	8.4	10.3
--Minor exports net rate	7.9	9.9	9.7	11.2	11.7	12.1
<u>Annual percentage rate of change in prices</u>						
--Wholesale prices	6.6	4.7	20.8	5.8	17.4	6.9
--Consumer prices	10.6	-1.2	14.9	5.6	18.3	7.7

x: Refers to 1967 through 1969 only

Sources and Method: Basic trade and national accounts data obtained as in Table I-1. "De facto coffee rate" calculated comparing coffee prices in Colombia and in New York, taking transpost costs into account. "Average import rate" obtained from IMF-IFS and BdlR-CN. "Minor exports net rate" calculated as in Chapter III. Price data obtained from IMF-IFS

Coffee recovery and the threat of a second world war first, then the war, and later the circumstances of post war 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. The index for the real 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 to the nominal rate, that index fell further to 54 in 1950, roughly the 1929 level. As it was probably the case in many other Latin American countries, the nineteen fifties opened with exchange rates which had gradually, almost unnoticedly, become "overvalued" during the nineteen forties, as nominal rates froze while domestic inflations advanced faster (but not that much faster in any given year) than in the United States.

The adjective "overvalued" is one to be used with care at all times, but particularly so in Colombia. There is probably no (real) exchange rate observed in Colombia during 1925-70 which could not have been turned into an "equilibrium" one by the appropriate choice of a coffee dollar price, even limiting possible choices to the range 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 controls.<sup>9</sup> For the whole 1930-68 period, there has been in fact a significant negative correlation between the real import exchange rate and the terms of trade, for a given year 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 while, as pointed out earlier, the Colombian coffee terms of trade (international) declined when the years 1948-70 are considered as a group, they show a significant positive trend, or at worst no trend, when all of the years since 1925 are taken into account.<sup>10</sup>

The early post war years, going 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 percent (the corresponding figure for 1925-45 is 4.1 percent, at a time when population was expanding at an annual rate of 2.1 per cent). As current dollar coffee prices doubled between 1945 and 1948 and tripled between 1945 and 1950, the expansion of absorption must have been higher than real GDP growth.

The export-led or coffee-fueled prosperity, aided by the quietest and least expected post war devaluation, in March 1951 (leading to a 28 percent 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. So in spite of an import exchange rate which in real terms was still substantially cheaper than the rates of the nineteen thirties, the first half of 1954 saw the elimination of the prohibited import list and the most liberal import regime witnessed in Colombia since 1929. It appears, however, that import controls and regulations were used even during those years for specific, ad-hoc protectionist purposes.

A sharp drop in coffee prices in mid-1954 from the astronomical levels reached earlier that year, even though coffee prices remained at historically high levels, and the high 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.

First, during early 1955, stamp taxes were imposed on imports, graduated according to the degree of "essentiality" of those imports. Later on 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 benefitted 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.

It may be seen in Table I-2 that although exports and imports remained during 1955 and 1956 at high levels, GDP growth slowed down, even though that of manufacturing held up. The 1955-56 rate of capital formation, buttressed by massive imports, reached 24 percent of GDP (at 1958 prices), the highest average for the period under study. The investment rate in machinery and equipment is particularly noteworthy. Table I-2 also shows that in spite of the creation of a free market for some imports, the real average import rate declined during 1955-56 relative to 1950 through 1954; the real rate applicable to minor exports, however, improved. It can also be seen that large imports did a fine job in keeping down price level rises.

Policy and Subphases: The 1957-58 Crisis

Economic conditions during early 1957 were of the sort which 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 payment 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.

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, 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 decade of the nineteen fifties 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 real net change against minor exports was even higher, not only because of the acceleration of Colombian inflation, but also due to the imposition of emerging export taxes to finance the servicing of the foreign debt 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 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 nineteen fifties and early sixties 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 which 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. Echoes of such a view, which under Colombian circumstances of those years can at best be regarded as premature, are to be found in more recent criticisms of export-promotion schemes. Incidentally, many of those who worry about the inefficiencies of "excessive" export incentives simultaneously argue that the supply of those exports is price-inelastic.

The stabilization efforts following June 1957 also highlighted a policy problem which has persisted, although in a reduced way, even to the present. 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, since June 1957 increasing use was made of advance import requirements not only as a way to reduce import demand, but also to control the growth in the money supply. As those deposits grew, the authorities found themselves increasingly "locked in" into a rigid and cumbersome situation.

Pressure from the politically-powerful coffee growers resulted in an increase in the real de facto coffee exchange rate (of about 18 percent between 1955-56 and 1957-58), even in the midst of gloomy prospects in the world coffee market. This experience illustrates the political difficulties which traditionally have limited the freedom of the Colombian policy maker 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.

In spite of these difficulties and ambiguities, and in spite of dollar coffee prices which during 1957-58 were 15 percent 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, inaugurated in August 1970, was to inherit, as President Lleras Camargo did in 1958, a smoothly going concern.

The stabilization plan was unable to contain an average annual rate of inflation of around 15 to 21 percent during 1957-58. Given the magnitude of the devaluation of the average import rate, as well as the clumsiness of the monetary policy tools and the degree of adjustment sought in the real economy, those rates do not appear unreasonable and were clearly on the decline when the new President was inaugurated. The real average import rate rose by an impressive 53 percent between 1955-56 and 1957-58, as shown in Table I-2, and import and exchange controls were rationalized, but remained very tight. The austerity regarding imports drove their average dollar value during 1957-58 to one-third below their level in 1955-56; restrictions on capital good imports appear to have been unusually severe, and the rate of capital formation in machinery and equipment, measured as a percentage of GDP at 1958 prices, 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.<sup>11</sup> It is curious that construction and some services performed more poorly than import-intensive manufacturing. Luckily, the crops appear to have been good during the stabilization plan.



The immediate cause of the payments crisis, i.e., the commercial arrears accumulated during 1955-56, had been either paid off or re-financed by the inauguration of the new President. In spite of lower coffee earnings, Colombia generated during 1957-58 a current account surplus, 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 I-3, 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 for Progress".

#### Policy and Subphases: Three 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. Those episodes deserve a special chapter, so this section will be limited to discussing a few key trends and themes of policy during the three first presidencies of the National Front, touching upon those dramatic events only lightly.

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

(a) Import "liberalization", in the sense of hoping to meet all "reasonable" requests for imported capital and intermediate goods, as well as raw materials. The notion of allowing imports which competed with local production, and/or "luxury" good imports, even with stiff tariffs, but without prior import permits was seldom popular and even more rarely became a policy objective.

Table I-3

The Colombian Balance of Payments, 1957 through 1969

(Annual Averages, Current Million Dollars)

	1957 and 1958	1959 through 1962	1963 through 1966	1967 through 1969
Coffee exports	378	317	366	352
Exports of petroleum products	69	70	79	51
Non-monetary and monetized gold	---	---	11	7
Other merchandise exports, including non-registered	<u>124</u>	<u>107</u>	<u>106</u>	<u>203</u>
Merchandise exports, f.o.b.	570	494	562	613
Merchandise imports, f.o.b.	-418	-492	-537	-576
-- <u>Trade Balance</u>	<u>153</u>	<u>2</u>	<u>25</u>	<u>37</u>
Transport receipts	na	na	58	78
Travel receipts	na	na	26	48
Other receipts from services and transfers	na	na	41	71
Transportation payments	na	na	-85	-106
Travel payments	na	na	-46	-63
Other payments for services and transfers, excluding investment income	<u>na</u>	<u>na</u>	<u>-85</u>	<u>-100</u>
-- <u>Net services, excluding investment income</u>	<u>-38</u>	<u>-41</u>	<u>-91</u>	<u>-72</u>
-- <u>Net payments for investment income</u>	<u>-44</u>	<u>-47</u>	<u>-80</u>	<u>-125</u>
<u>Balance in Current and Transfer Account</u>	<u>71</u>	<u>-85</u>	<u>-146</u>	<u>-160</u>
Net long term private capital	-13	29	107	106
Net short term private capital	-8	5	12	-15
Private commercial arrears and net credit from commercial banks	-104	4	19	22
Net grants and official capital	----	25	44	91
Errors and Omissions	-34	16	-42	6
<u>Net "autonomous" Capital</u>	<u>-159</u>	<u>79</u>	<u>140</u>	<u>210</u>
Net Loans and credits received by BdLR	97	-18	8	-29
Net IMF Account	3	8	3	16
BdLR gold and foreign exchange, net of payment agreements liability	-12	17	-4	-38
<u>Net "compensatory" Capital</u>	<u>88</u>	<u>7</u>	<u>7</u>	<u>-51</u>

Sources and Methods: Adopted from data in the IMF's Balance of Payments Yearbook,

several issues. Where data were not available in directly comparable form, the initials "na" were used. Minus signs refer to debits, positive figures are credits.

Therefore, under "compensatory" capital, a negative sign indicates a build-up of reserves. Note that "net long term private capital" includes loans received by the Colombian private sector from institutions such as the IBRD, IADB and USAID.

- (b) Stable, "non-inflationary", "non-speculative", exchange rates.
- (c) Sharply growing minor exports
- (d) Substantial inflows of concessional long term capital inflows ("aid"), 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 and U.S. commercial banks.
- (e) Keeping down the de facto coffee exchange rate, to reduce excessive domestic coffee stocks, promote agricultural diversification, while increasing public revenues and dampening inflationary credit requests from the federation of coffee growers.

The coordination of just the various policy instruments relevant for the balance of payments was a difficult task during most of the years under study, as frequently each policy instrument was jealously guarded by separate bureaucratic units. 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 hand, 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<sup>12</sup>; 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.

A further general remark should be made regarding the sociopolitical milieu in which trade and payments policies are adopted in Colombia. Although since 1958 Colombia has been governed by constitutional civilian regimes, 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<sup>13</sup>, even though the "elitism" gradually declined throughout the nineteen sixties, and is now under serious political attack. Income distribution is sharply skewed; it is estimated that in 1961 the top 10 percent of income earners received 42 percent of the country's total personal incomes, while the bottom 50 percent of income earners received only 18 percent of that income. In 1962 only 34 percent of children aged 5 to 19 were in primary and secondary schools (in 1950 the corresponding figure was 24 percent). Other social indicators confirm the picture of inequality and severe poverty for families at the bottom 50 percent 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, on average, in the economy. But it should be borne in mind that, especially in the short and medium run, much of the policies discussed in these and later chapters touch only marginally the welfare of large parts of the Colombian masses. And it is not always clear whether a priori desirable policies affect positively or negatively 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) which 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. As already noted, the presidency of Alberto Lleras Camargo opened not only with considerable national and international goodwill, but also with the 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. As shown in Table I-2, higher GDP growth rates were indeed achieved, and merchandise imports, although still below the 1955-56 levels, rose sharply over the depressed 1957-58 figures, and were comparable to those averaged during 1950 through 1954. Coffee prices, however, continued their decline; their average for 1959 through 1962 was 37 percent 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 (found both under net grants and official capital, and under net long term private capital in Table I-3).

The more generous granting of import licenses, which started in 1959, was accompanied by a stickiness in the average exchange rate applicable to imports. Earlier intentions to gradually adjust that rate, aiming at an eventual unification of the "certificate" with the free market were quietly dropped. The average import rate, expressed in real 1963 prices, dropped from 10.1 Pesos in 1958, to 9.2 Pesos in 1959, to 9.1 Pesos in 1960 and to 8.7 Pesos in 1961. Fears of reviving inflationary pressures blocked a more

vigorous adjustment of the import rate. Inflation was in fact kept at an annual rate of less than 6 percent during 1959 through 1962.

The real net exchange rate applicable to minor exports, however, remained at levels superior to those of 1950 through 1958, 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 to most 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, since January 1959, after a period of association 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 16 quarters of 1959 through 1962 was about 6 percent. Neither the extent, nor the contribution toward stability, if any, of sporadic Central Bank intervention in the free market during this period are 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 minor exports was insufficient to face growing import demand, and the dreary process of denials, heroics and increased Bogota-Washington shuttles

clearly pointed to an impending devaluation of the major import rate. The trend toward some "liberalization" of import licensing observed during 1959 through 1961 was clearly 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 insatiable 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 "auction" or "certificate" 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 politico-economic program was to play an important role during the following years, hindering liberalization efforts. Reasons for the failure of this devaluation will be discussed in a later chapter; it is enough to point out here that a sharp domestic inflation during the early part of 1963 wiped out practically all of its incentive effects, so that the real average import exchange rate for 1963 was only two percent higher than that for 1962, and of course below the 1958-60 levels. The gloomiest predictions of those who had opposed devaluation 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 net real average



exchange rate applicable to minor exports during 1963 was 13 percent below what it had been during 1962.

Under these circumstances, expected post-devaluation import liberalization moves remained feeble, and it was not long before rumors of a new devaluation began to circulate. 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 90 days (except for imports from LAFTA). The President, however, burnt 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 near 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, so long as their import content did not exceed 50 percent. If it did, those exports were to receive the rate of 9 Pesos.

Once established, 13.5 took on some magic. It is said that the President was persuaded that a gradual transferring of imports from the 9 Pesos ("preferential") rate to the new 13.5 Peso ("intermediate") rate, 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 13.5 Peso rate 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 requirement. This was indeed the beginning of the most ambitious liberalization attempt of Colombia's post war economic history, which in turn provided the background to the dramatic confrontation between a new Colombian government and foreign creditors, over exchange rate policy, which took place in November, 1966. The import liberalization program advanced boldly, so 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 upwards, to take into account the new situation, almost unique in Colombia's post-1929 economic history, and only comparable 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: the value of merchandise imports went from \$111 Million in the third quarter of 1965 to \$193 Million in the third quarter of 1966.

Taken as a whole, the years 1963 through 1966 witnessed a slowdown of GDP growth, as shown in Table I-2, with the rates of expansion of manufacturing, construction and type I services showing the more significant declines, even though both the value of exports and imports recovered somewhat from the depressed 1959 through 1962 levels. In spite of the hesitations over incentives, minor exports continued to expand. 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 average real exchange rates for coffee, imports and minor exports during 1963 through 1966 were fairly close to those of 1959 through 1962.

The Lleras Restrepo Presidency. The new 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 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 basically pleaded for time to first get a firm grip over 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 post-liberalization boom.

Aid, it added, was supposed to help out precisely in times such of 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 a later chapter; here it will be sufficient to note that in an extraordinary television appearance President Lleras Restrepo on a Tuesday, November 29, 1966, announced to the nation a rejection of the demands of the by then united foreign creditors, the 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 attention to the preparation of what was to become Law 444 of March 22, 1967. That Law 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 post war period of policy stability. A key 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 and/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. Especial 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 percent and later lowered to 20 percent. Previously, coffee exports received a special, fixed exchange rate. In other words, after March 1967 coffee exports developed a vested interest in the continuation of the upward crawl of the certificate rate, while before they were primarily interested in just a favorable coffee rate.

Law 444 replaced previous fiscal incentives for minor exports, under which minor exports reduced the income tax liability (Law 81 of 1960), with the simpler and more general tax credit certificate (CAT). The CAT given to minor exporters was set at 15 percent 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 in the Chapter on minor exports. The new law also created the Export Promotion Fund (PROEXPO), with wide powers and attributes to carry out the role embodied in its title.

In the field of general exchange and import controls, Law 444 tidied up 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 overpayments for royalties and foreign patents foreshadowed and in some respects, inspired the tough rules adopted by the Andean Common Market during 1970 and 1971.

Simultaneously with the preparation of Law 444, the Lleras Restrepo administration struggled to get a firm grasp on coordinate 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 has gone on to this day.

That liberalization trend, 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 (minor) 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. The trade and payments policies of the Lleras Administration, in fact, have been continued under

the Misael Pastrana Borrero administration, which has also maintained the liberalization trend. How the restrictive system looked in 1970 and 1971 will be a subject for a later chapter.

During 1967 through 1969 the GDP growth rate, as shown in Table I-2, rose to a level unmatched since the 1950 through 1954 subphase; preliminary data for 1970 and 1971 suggest that growth rate (5.6 percent per annum), was exceeded during both years. The acceleration of manufacturing growth, however, seems relatively modest, and was exceeded by those of construction and, notably, primary production. (Data on manufacturing, as well as those for capital formation, particularly in machinery and equipment, in fact look a bit peculiar for 1966 through 1969, and surprisingly low.) The 1967 through 1969 aggregate marginal capital-output ratio was the lowest recorded for any of the subphases in Table I-2; it may be more accurate to say that it returned to roughly the same levels reached during 1950 through 1954 and 1959 through 1962. Other information, including ratios of value added to installed horsepower capacity in manufacturing, computed by John Todd, point to falling capacity utilization during 1957-58 and during 1963 through 1967.

On average, for 1967 through 1970, dollar coffee prices were roughly at the level reached during 1963 through 1966; the dollar value of minor exports, however, about doubled between those two periods. Helped by minor exports and aid disbursements merchandise imports exceeded the average dollar values reached during 1955-56. As shown in Table I-3, this time import expansion 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 at the end of 1970. Consolidating errors and omissions, net short term private capital, and commercial arrears and net credit from commercial banks, found in Table I-3, it may be seen that their sum went from a net debit of \$11 Million a year during 1963 through 1966, to a net yearly credit of \$13 Million in 1967 through 1969.

The 1967 through 1970 averages for exchange rates for both imports and minor exports surpassed those of all other subphases shown in Table I-2. Furthermore, their rise was gradual, popular calculations<sup>14</sup> to the contrary notwithstanding. The Colombian inflation during those years dropped to about the "normal" levels of 1950 through 1954, and 1959 through 1962, and was not much ahead of the inflation registered in industrial centers during the same years.

All of this looks like a happy ending to our post war summary narrative. Indeed, at the moment Colombia looks embarked on the reasonably steady growth path on which it was launched by Law 444. Our last chapter will deal with possible obstacles, some not strictly economic, as well as with proposals to make that path higher. But before we get there many details need filling in.



## Footnotes to Chapter I

\* This essay is part of a project studying major characteristics of the Colombian international trade and payments system. In turn, that project is part of the NBER Exchange Control around the World super-project. Annexes A and B present a list of abbreviations used in this and following chapters, and a list of principal events, respectively. Albert Berry, Rodrigo Botero, Elizabeth S. Burgess, Mary K. Downey, José Francisco Escandón, Stephen Kadish, Christina Lanfer and Carlos Sansón, were especially helpful to me in the preparation of this essay. But they may not agree with my opinions and judgments, and certainly should not be held responsible for how I utilized their kind support.

1 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, New Jersey: 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 Book Company, 1967).

2 See Alasdair I. Macbean, Export Instability and Economic Development (Cambridge, Massachusetts: Harvard University Press, 1966).

3 This is also true for several other Latin American countries. See my "Planning the Foreign Sector in Latin America", The American Economic Review, Volume LX, Number 2, May 1970, especially pp. 170-74.

4 See Lauchlin Currie, "The Exchange Constraint on Development--A Partial Solution to the Problem", The Economic Journal, Vol. 81, No. 324, December 1971, pp. 886-904.

5 Three import price indices were tried; those of UNECLA (SB and DANE) for the whole period, those appearing for the post war in IMF-IFS, and, linked to those of IMF-IFS, the ones found in UA, pp. 212-13 (estimates of

William Paul McGreevey). Current export values are found in the same sources. The highest t-statistic (1.72) was that for the coefficient of the percentage changes in the real value of exports contemporary with the change in GDP, in the regression covering 1929 through 1968. But the absolute value of even that coefficient is very small.

6 The series used, labelled "Capital Goods Import Quantum (I)", is that employed in constructing national accounts estimates for fixed investment. UNECLA-SB provides other series for imports of capital goods (available since 1950 only at current dollar prices). The  $R^2$  between these two series is 0.53 (a trend term would improve the fit substantially). A third series is given in BdlR-1AGJD-XLV and XLVI, p. 167, also at current dollar prices. The  $R^2$  between this series and the second one is 0.87; and with the first series the corresponding  $R^2$  is 0.51.

7 For an elaboration of this point see my Essays on the Economic History of the Argentine Republic (New Haven: Yale University Press, 1970), especially pp. 79-85.

8 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: U.S. Government Printing Office, 1970), Statistical Tables. The Colombian price indices are rough.

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

10 The coffee terms of trade calculated by UNECLA (SB and DANE) show a positive coefficient, of 0.4 percent per year, for the time trend, but with a t-statistic of only 1.65. The terms of trade found in UA, pp. 212-13,

linked with those of IMF-IFS show an annual rate of improvement of 2.1 percent per annum; that coefficient has a t-statistic of 5.5. Both estimates were obtained by fitting semi-logarithmic equations to all observations during 1925 through 1968.

11 Compare, as Jere Behrman would say, Colombian GDP behavior with that of Argentina, where real GDP fell in 6 years found 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 percent.

12 The Committee of Nine report, distributed by the Pan American Union, was entitled Evaluación del Programa General de Desarrollo Económico y Social de Colombia. 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 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.

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

14 One often sees calculations comparing the exchange rate "crawl" only to the rise in Colombian prices, neglecting inflation in the rest of the world. This is sometimes defended with the argument that as the Colombian exchange rate is overvalued anyway, any argument to accelerate its upward "crawl" is to be welcomed and used, presumably on unsophisticated policy makers. I doubt many policy makers would swallow such a gross calculation; at any rate, that kind of tactic will not serve an educational purpose, and in the long run it could very well backfire, when technicians are found

out to be, after all, not such objective and neutral outliners of options open to the politician.

## Annex A to Chapter I

### Abbreviations

- UNECLA: United Nations Economic Commission for Latin America. When followed by SB, the reference is to one of that organization's periodical publications, the Statistical Bulletin for Latin America. When followed by DANE, it refers to the statistical appendix of ECLA's Colombian study, reprinted in DANE's Boletín Mensual de Estadística, No. 226, 1970, pp. 115-189.
- DANE: Departamento Administrativo Nacional de Estadística. When followed by BME, the reference is to one of that organization's periodical publications, the Boletín Mensual de Estadística.
- IMF: The International Monetary Fund. When followed by IFS, the reference is to one of that organization's periodical publications, the International Financial Statistics.
- UA: Publication edited by Miguel Urrutia and Mario Arrubla, Compendio de Estadísticas Históricas de Colombia (Bogotá DE, 1970; Universidad Nacional de Colombia).
- BdlR: Banco de la República (Central Bank). When followed by CN, the reference is to the national accounts (Cuentas Nacionales) published by that institution. When followed by IAGJD, the reference is to the Informe Anual del Gerente a la Junta Directiva, published as a rule annually. The specific publication is identified by roman numerals referring to the order of the report beginning with the year of the Bank's founding.
- IBRD: The International Bank for Reconstruction and Development (the "World Bank").
- IADB: The Inter-American Development Bank
- USAID: The Agency for International Development of the United States government.

LAFTA: The Latin American Free Trade Association.

CAT: Certificado de Abono Tributario, or Tax Credit Certificate.

PROEXPO: Fondo de Promoción de Exportaciones, The Export Promotion Fund.

## Annex B to Chapter I

### Principal Events

September 1931: Widespread exchange controls and trade restrictions introduced.

April 9, 1948: The assassination of Jorge Eliécer Gaitán, leader of the Liberal Party, provokes wild urban riots, and is followed by rural violence, which lasts well into the nineteen fifties.

December 1948: Exchange restrictions revised.

July 10, 1950: Exchange restrictions revised.

March 20, 1951: Except for a prohibited import list of some 1,200 specified luxury or locally produced items, practically all licensing restrictions on imports were removed, leaving only a prior registration procedure for permitted imports. Basic exchange rates depreciated from 1.95 to 2.50 Pesos per U.S. dollar. Multiple exchange rates considerably simplified, but still resulted from the application of exchange taxes and a mixed effective rate for coffee exports.

August 1, 1952: Export voucher system introduced for minor exports; vouchers which are negotiable, can be used to import previously prohibited items.

September 6, 1952: The house of Carlos Lleras Restrepo, Liberal Party Leader, set on fire, marking a further deterioration of Liberal-Conservative rivalry.

June 13, 1953: General Gustavo Rojas Pinilla assumes the presidency, with the backing of the Armed Forces and of a good share of public opinion.

February 19, 1954: The prohibited import list is eliminated. Throughout most of 1954 a gradual relaxation of import and exchange restrictions takes place, but by October some restrictions are re-introduced.

In February a de facto ceiling of 3.50 Pesos for the rate applicable for minor exports is established.

March 1954: Colombian coffee reaches 99 cents (of U.S. dollar), a pound in international markets; by August it is down to 67 cents.

August 1954: A backlog of commercial arrears owed to foreign suppliers begins to be noticeable. In October the granting of exchange for import payments is made contingent upon arrival of the merchandise to Colombia.

February 16, 1955: Imports reclassified and subjected to ad valorem stamp taxes, as follows:

Preferential,	3%,	(raw materials for essential industries)
Group I,	10%,	(other raw materials and essential products)
Group II,	30%,	(essential durable and semidurable goods)
Group III,	80%,	(less essential goods)
Group IV,	100%,	(specified non-essential goods)
Prohibited,		(luxury goods)

May 13, 1955: A broad free market is introduced. Imports in Groups II, III and I and IV and most non-trade transactions, shifted to new free market (from official rate). By december 31, 1955 the free market rate reaches 4.2 Pesos, compared with 2.5 Pesos for the official rate.

November-December 1956: Import restrictions intensified; commercial arrears continue to grow. A free exchange certificate market replaces the free market. The fluctuating rate for exchange certificates reaches 6.5 Pesos by December 31, 1956; that market shows great instability.

May 10, 1957: General Rojas Pinilla ousted; a provisional government is formed. The liberal and Conservative parties agree on a 16 year pact, the National Front.



June 1957: Stabilization program adopted to arrest inflationary pressures and restore payments equilibrium. A Superintendency of Imports is created to review import license requests; a prohibited list, a restricted list and a free group are maintained. New simplified exchange system introduced. A new "certificate market" is put into operation, together with a free market. Both consolidate sharp devaluations; on December 31, 1957 the fluctuating certificate rate was 5.4 Pesos per U.S. dollar, while that for the free market was 6.2. The quotation for the "certificate" rate is theoretically determined at auctions held by the Bank of the Republic. Most commercial arrears settled by the end of 1957. Net effect of exchange reforms of June 1957 is, however, detrimental to the rate applicable to minor exports, which are switched from the free to the new certificate market. Progressively tighter advance import requirements observed since June 1957.

March-April 1958: Exchange system modified; negotiable exchange certificates no longer issued against proceeds of exports, whose rate is now pegged at 6.1 Pesos (less appropriate export tax), although periodic changes in this and other pegged rates are contemplated, in principle.

August 7, 1958: President Alberto Lleras Camargo inaugurated, following his election in May.

January 16, 1959: New changes in the exchange and payments system. A new, more favorable rate is established for minor export proceeds, which would vary in line with fluctuations in the free market rate.

May 1959: A more comprehensive custom tariff with higher import duties introduced.

February 1960: Signature of the Treaty of Montevideo, creating the Latin American Free Trade Association. The Treaty entered into force in June, 1961.

April-May 1960: Minor devaluations in the official buying and selling rates, but spread between official and free rates widens. Official rates are rigidly pegged, as 6.7 Pesos, while free rate undergoes sharp fluctuations.

January 13, 1962: The Colombian government requests that the Committee of Nine of the Alliance for Progress study and report on its first General Economic and Social Development Plan.

August 7, 1962: President Guillermo León Valencia inaugurated, following his election in May.

September 1962: Virtually all imports made subject to prior license.

Liberalization trend of 1959-61 reversed during 1962.

September 1962: The International Coffee Agreement is signed, after two years of negotiation. It began to operate in 1964.

November 1962: Early in the month merchandise included in the import free list and the prior licensing list was transferred temporarily (for six weeks) to the prohibited list. On the 20th of the month, the "auction" rate was allowed to depreciate from 6.7 to 9.0 Pesos per U.S. dollar. A free market is maintained; at the end of December 1962 that rate was 11.1 Pesos per U.S. dollar.

January 11, 1963: The Bank of the Republic begins pegging the free market rate, at 10 Pesos per U.S. dollar.

September 1963: Powers of monetary management transferred to new Monetary Board, whose majority is made up by Cabinet Ministers.

July 17, 1964: Monetary Board given legal authority to change the certificate system and the auction rate.

October 25, 1964: The Bank of the Republic ceases pegging the free exchange market. By December 31, 1964, the free market rate reaches 12.8 Pesos. Minor exports continue to receive free market rate.

December 1, 1964: Serious consideration given to new devaluation, but political resistance is too great. Import licensing becomes more strict; free import list eliminated.

June 30, 1965: Exchange rate for minor exports, previously equal to free market, pegged at 13.5 Pesos. Free market rate climbs above 19 Pesos in July and August. Pressures for new devaluation persist.

September 1965: A number of imports are freed from licensing requirements, if paid for at the new "intermediate" official exchange rate of 13.5 Pesos; other remained subject to licenses, but obtained "preferential" rate of 9 Pesos. Plans for further import liberalization announced. The official buying rate for coffee exports is raised from 7.7 Pesos to 8.5 Pesos.

October 1965: Progressive reductions of advance import deposits started; it went on until August 1966, when original schedule was stretched.

November 1965: More imports transferred to "intermediate" exchange rate, and freed from Licensing requirements.

January 1966: A third list of Liberalized imports issued.

February-March 1966: Three further lists of liberalized imports are issued.

July-August 1966: All imports placed under the intermediate rate of 13.5 Pesos; most imports freed of licensing requirements. Free exchange market continued for some invisibles and capital transactions; free rate appreciates between September 1965 and mid-1966.

August 7, 1966: President Carlos Lleras Restrepo inaugurated, following his election in May.

Last quarter of 1966: New York coffee price falls from 50 cents a pound during the first quarter of 1966 to 45 cents during the last quarter of 1966.

November 29, 1966: All imports again require prior licenses; operations in the free exchange market suspended. Free market replaced by capital market, with rate pegged at 16.3 Pesos. President Lleras Restrepo rejects pressures from the IMF and foreign creditors to devalue. All Colombian residents to declare foreign exchange holdings to Exchange Control Office. Price controls imposed.

January 27, 1967: Previous import deposit rate requirements brought up to only 40 percent below their level in September 1965. Further raised on February 9, 1967.

March 22, 1967: Decree-Law No. 444 is published, restructuring the whole field of exchange and foreign trade. It sets up a ("crawling") exchange certificate market rate and a capital market rate. Import control regulations maintained. Detailed and rigorous regulations are also established over direct foreign investment.

Post-November 1967: Concern expressed about (temporary) slowdown in the upward crawl of major ("certificate") exchange rate.

May 1968: Free import list regains some significance.

June 1968: The capital and certificate exchange rates are unified.

August 22-24, 1968: His Holiness Pope Paul VI visits Colombia.

February 1969: Previous import deposit rates, generally lowered during 1968, further reduced.

June 11-13, 1969: President Carlos Lleras Restrepo visits the United States.

September 1969: A sharp upswing in dollar coffee prices starts.

October 22, 1969: The Andean Pact enters into force.

March 16, 1970: The import free list, comprising about 100 tariff items, was expanded by 51 tariff items.

August 7, 1970: President Misael Pastrana Borrero inaugurated, following his election in April.

September 1970: Further expansion of the import free list; for 1970 as a whole items in the free list accounted for about 25 percent of reimbursable imports. Throughout the year many items were also switched from the prohibited to the prior license list and advance import deposit requirements were lowered.

October 15, 1970: The CAT waiting period reduced from 12 to 9 months.