IMPLEMENTATION OF DEVELOPMENT PLANS: PROBLEMS AND EXPERIENCE

World Economic Survey
1966—Part One

UNITED NATIONS

Department of Economic and Social Affairs

IMPLEMENTATION OF DEVELOPMENT PLANS: PROBLEMS AND EXPERIENCE

World Economic Survey 1966 — Part One

UNITED NATIONS
New York, 1967

NOTE

Symbols of United Nations documents are composed of capital letters combined with figures. Mention of such a symbol indicates a reference to a United Nations document.

E/4363/Rev.1
ST/ECA/99

UNITED NATIONS PUBLICATION

FOREWORD

This report, *World Economic Survey, 1966*, is the nineteenth in a series of comprehensive reviews of world economic conditions published by the United Nations. It is issued in response to General Assembly resolution 118 (II), in which the Secretary-General was requested to prepare an annual review and analysis of world economic conditions and trends. The report is intended to meet the requirements of the Economic and Social Council and other organs of the United Nations for an appraisal of world economic conditions which may serve as a basis for recommendations on economic matters. It is also intended to stimulate interest in and discussion of international economic problems among a more general public audience.

Each year since 1955, the *World Economic Survey* has contained a study of a particular problem concerning economic development. Among the subjects examined have been economic growth in the first post-war decade, balance of payments problems in relation to economic growth, inflation, post-war commodity trade and policies, experience and policies relating to investment and saving, industrialization and economic development, foreign trade and economic development, the appraisal of development plans and the financing of economic development.

Part One of the present *Survey* contains a series of papers dealing with problems and experience in the implementation of development plans. The subject of plan implementation has figured prominently in recent discussions in international forums. It has been emphasized that while many developing countries have drawn up plans few have been successful in implementing them. If the objectives of economic development to which the world community has attached great importance are to be achieved, much attention will have to be given to bridge the gap between plan formulation and plan implementation. In view of the urgency of the problem, the Committee for Development Planning, which was established in 1966 by the Economic and Social Council, has decided to place major emphasis in its own work on the problem of plan implementation. The Committee's report on its second session, held in Santiago, Chile, in April 1967, provides both an analysis of and recommendations concerning plan implementation, with special reference to Latin America.[1] A number of aspects of the subject were also examined by several members of the Committee in individual papers prepared by them for that session; those papers are being published in a volume entitled *Planning and Plan Implementation*.[2]

The first four chapters of part One of the present *Survey* discuss some aspects of plan implementation in developing countries. These are followed by three chapters which review certain aspects of the experience of the centrally planned economies that may be relevant to the problems of plan implementation in developing countries. It is hoped that all these chapters, together with the report of the Committee for Development Planning and the volume *Planning and Plan Implementation* will contribute to a broad public discussion of the important policy issues involved.

Part Two of the *Survey*, which is issued as a separate volume, deals with the salient features of the world economic situation. It covers the events of 1966 and early 1967 and summarizes the principal developments in, first, the world economy as a whole and, then, in each of the three broad groups of countries constituting the world economy—namely, the developed market economies, the centrally planned economies and the developing countries. It incorporates information provided by Governments in response to the Secretary-General's questionnaire on economic trends, problems and policies circulated in November 1966.

The *World Economic Survey* is prepared in the Centre for Development Planning, Projections and Policies of the Department of Economic and Social Affairs of the United Nations Secretariat.

---

[1] *Official Records of the Economic and Social Council, Forty-third Session, Supplement No. 7* (E/4362).

[2] United Nations publication, Sales No.: 67.II.B.14.

CONTENTS

List of Tables

Explanatory notes

The following symbols have been used in the tables throughout the report:

Three dots (. . .) indicate that data are not available or are not separately reported

A dash (—) indicates that the amount is nil or negligible

A blank in a table indicates that the item is not applicable

A minus sign (-) indicates a deficit or decrease, except as indicated

A full stop (.) is used to indicate decimals

A comma (,) is used to distinguish thousands and millions

A slash (/) indicates a crop year or financial year, e.g., 1960/61

Use of a hyphen (-) between dates representing years, e.g., 1961-1963, signifies the full period involved, including the beginning and end years.

Reference to "tons" indicates metric tons, and to "dollars" ($), United States dollars, unless otherwise stated.

Annual rates of growth or change, unless otherwise stated, refer to annual compound rates.

Details and percentages in tables do not necessarily add to totals, because of rounding.

The designations employed and the presentation of the material in this publication do not imply the expression of any opinion whatsoever on the part of the Secretariat of the United Nations concerning the legal status of any country or territory or of its authorities, or concerning the delimitation of its frontiers.

A. *Some aspects of plan implementation in developing countries*

Chapter I

SOME CONDITIONS FOR THE EFFECTIVE IMPLEMENTATION OF PLANS

While a great many developing countries have drawn up development plans in recent years, comparatively few have experienced much success in achieving their targets. The fact that plans have often not accomplished what they set out to do is commonly equated with a failure in plan implementation. This simple measure of success or failure, though not without validity, is subject to some qualifications.

Certainly, it would be everywhere accepted that even the best laid plans sometimes fail for reasons that have little or nothing to do with planning but a great deal to do with human fallibility in predicting the course of future events. In some instances, political upheaval has rendered national planning largely irrelevant; or an unexpected deterioration in world market conditions or a series of bad harvests has radically altered the economic situation; or external aid for development programmes has unexpectedly failed to materialize. No one would deny that the effects of such events have to be discounted in appraising the success or failure of a plan.

Even when allowance has been made for such unforeseeable events, the frequent discrepancy between plans and performance cannot always be ascribed to a failure in implementation. Some of the disappointment with progress in implementation has undoubtedly been misplaced. In many developing countries, ambitious national plans have been drawn up but these have outreached the power of Governments to implement them. And where plans require actions that are beyond the power of the executing authorities to command, the fault surely lies not in the failure to implement but in the lack of realism of the plans.

The tendency of plans to outreach the power of most Governments in developing countries has been, in large measure, a consequence of the emphasis on comprehensive planning. It is relevant to recall that the movement towards the construction of plans with a comprehensive and consistent set of targets arose from the criticism of earlier post-war plans that they dealt only with particular sectors or with groups of public investment projects and that the proposals for these sectors or projects could not be properly evaluated in the absence of a framework for the economy as a whole. For this reason, plan formulation in more recent years has been concerned with the construction of an economy-wide perspective. This is all to the good. The elaboration of a comprehensive framework is certainly needed as a guide to the design of development policy since it permits, first, a more systematic exploration of the kinds of changes in the structure of production required to maintain or accelerate growth and, secondly, the identification of the actions that can be taken by government to bring about these changes. In the process, however, many of the quantified changes, which are more in the nature of forecasts and are not within the power of Governments to determine with any measure of certainty, have tended to assume the status of targets. It has been too easily forgotten that, in most of the developing countries, most agricultural and industrial production and a major part of investment are undertaken within the private sector; and while the influence which most Governments can exert on the private sector is not inconsiderable, it is not so great that it can in any way ensure that the necessary decisions will be taken. Thus, if plan implementation is taken to mean the execution of a programme of action designed to reach certain specified objectives or quantified targets, then in most developing countries the power of the Government to carry out comprehensive plans is circumscribed. In fact, their capacity to implement plans in this sense is limited largely to partial plans for the public sector.

This argument should not be pushed too far. In the present-day world, no sharp line of distinction between the private and the public sector can be drawn, and there are many shades of difference in the control or influence exerted by Governments not only among countries but also among activities within the same countries. Further, the argument does not mean that policies for influencing decisions within the private sector should not be designed within the framework of a perspective for the economy as a whole. But it is salutary to bear in mind that, in mixed economies with large private sectors, success or failure in the achievement of targets for the economy as a whole is not a fair measure of governmental performance in the implementation of plans; in this area, implementation has to be judged rather in terms of the effectiveness with which policies intended to influence private decisions have been designed and executed.

It is when a more modest and restrained definition is placed upon planning, as the design and execution of partial plans, that failure to realize objectives and targets can be more properly described as a failure in implementation. Even interpreted in this more limited way, however, experience in implementation has generally been disappointing. Many of the weaknesses have arisen at the various stages of execution and a number of these are discussed in other papers. But, particularly in countries making their initial attempts to plan, these weaknesses have also had their source in plan formulation.

Development planning has been defined as the planning of development policy. But it would appear that in their initial attempts to establish planning processes many developing countries have tended to lose sight of this aim. Perhaps as a consequence of preoccupation with the unfamiliar techniques of plan elaboration, planning has tended to be too largely identified with the task of preparing a comprehensive and consistent set of objectives and targets for the plan period. The plan has been drawn up by a group of technicians working in comparative isolation from the normal governmental processes; and instead of being an instrument for reaching policy decisions it has become an exercise in what might happen on the assumption, often implicit, that a whole array of changes in policies and institutions would be made.

Of course, it has not infrequently been true that the preparation of a plan document by a small technical group has largely satisfied political intentions; the plan has been meant as a vehicle for the statement of a political position, and not as an operational instrument. But when the plan is intended to guide policy decisions, it is clear that a quite different approach to plan formulation is called for. As will be illustrated below from the experience of countries with fairly well-established planning systems, it is essential to draw the various decision-making groups into the process of formulation so that, through consultation and agreement at the various decision-making levels, a programme of action for implementation of the plan might be evolved. In this sense, the effective implementation of plans begins at the stage of formulation.

It is certainly not to be pretended that the task of obtaining broad support and agreement for the actions required to implement a plan can ever be accomplished easily or without friction. It must embrace not only the various arms of government but also the different political and social groups in the nation, and it is therefore an exercise in political compromise. For those anxious to accelerate economic growth, however, a dilemma is always present which must somehow be resolved. While any plan which is more than a mere projection of past trends is bound to propose changes that modify existing social and institutional conditions, every plan has to be initiated and to find acceptance within these same conditions. A plan which fails to take account of the political realities presented by these conditions may not secure support for the policies necessary for its implementation. It may serve some educational role of long-run importance in changing the climate of political opinion; but it will not be a programme of action. At the same time, if it falls into the opposite error of proposing no lines of action which do not conform to "present political realities", it may fail in its intended purpose of promoting development. Some point of political balance has to be found between these two extremes.

The devising of plans which are politically realistic and yet effective programmes of development is a process which, though not assured, can be eased through the piecing together of suitable machinery and other arrangements to link the various decision-making groups. The machinery, moreover, must link planning and decision-making at the various political and administrative levels and in the various phases in execution of the plan. In a functioning planning system, the distinction between plan preparation and plan implementation is, in fact, more formal than real. Planning takes place at all levels from the initial preparation of a comprehensive framework down to the planning for construction of a specific project; and it takes place in all phases of implementation as medium-term plans are broken down into progressively shorter programmes of action. These procedures, however, can only be developed over time as attempts are made to construct and implement plans. While the capacity to formulate and implement plans may initially be very limited, it is only through attempts to plan that the machinery for planning can be put together.

In the sections that follow, an attempt is made to indicate briefly the relation the main decision-making groups bear to the planning process by illustration from the experience of several countries with fairly well-established planning systems. Though the emphasis throughout the discussion is on the problems of developing countries, examples from certain developed countries are also used to throw light on the issues involved.

THE ROLE OF THE EXECUTIVE

Having general responsibility for the framing and execution of policies, the executive head of government, together with his council or cabinet, stands at the centre of the whole planning process. In a formal sense, all the policy decisions undertaken within government in the course of plan formulation or implementation require the approval of the executive head, either directly or through his ministers. In more operational terms, however, the participation of the highest political authorities in planning is generally confined to major policy issues.

In the formulation of plans, the practice established in countries with some years of planning experience has called for participation by the executive heads at an early stage of preparation. A broad framework of possible targets and policies has been elaborated by the planning agency and submitted to the executive head and his council for consideration of the major alternatives and determination of the major objectives and lines of policy to be pursued. The technical work at this stage has usually not required extensive machinery or complex techniques; it has been at a fairly aggregative level, resting on analysis of general trends and prospects and the use of some simple model. In fact, a primary condition for the success of such work has been that it should pose the main alternatives and policy issues in forms that are clearly intelligible to the policy maker. The purpose has been to elicit discussion and initial decision on such issues as: the size of the public development programme, taking into account its implications for fiscal policy and the degree of dependence on foreign aid; the relative emphasis on agriculture, industry, infrastructure or the social sectors; the regional distribution of public expenditure; employment policy, or policies for institutional or administrative reform. Through consideration of such issues by the political authorities at this preliminary stage of plan preparation, some balance has been struck in the priorities to be attached within the plan to conflicting political and social objectives.

Illustrations of this procedure could be drawn from several countries, but mention may be made here of the examples of Pakistan and France. In Pakistan, when preparation of the medium-term plan is initiated, the Planning Commission prepares a "preliminary policy paper" which identifies broad policy objectives, estimates resources required for the plan, and makes tentative proposals regarding the size of the plan and the sectoral allocation of resources. That paper is circulated for comment to central ministries and provincial governments. In the light of these comments and of subsequent discussions with the ministries a paper setting out "guidelines" is prepared and submitted for approval to the National Economic Council, which is the supreme economic policy-making body and is chaired by the President.

In France, notably in connexion with the preparation of the fifth plan, the process of plan formulation has been initiated by the Planning Commission with the formulation of a number of variants for consideration by the Government. These have been progressively modified in the light of discussion by the executive and of the latter's decisions with respect to policies. In this way, the major "options" have been elaborated and these have been subsequently submitted to Parliament for its consideration and approval. These procedures have been designed to ensure that the possibilities of implementation would be considered in the course of plan elaboration and that the Government would have the opportunity to consider at an early stage the implications of the choices which it might make.

Thus, in these countries, at the preliminary stage of plan preparation the policy makers have been called upon to make certain decisions regarding major issues. Proposals regarding plan targets and policies, moreover, have been elaborated in sufficiently concrete terms so that these decisions have related to specific questions of plan content rather than to abstract issues of strategy. It is true that there is always a danger in such consultations between planners and the political authorities if they are held too early and too frequently. It may induce such a preoccupation among planners with present political realities that they cease to make the bold policy proposals for development which, as an advisory group, it is their function to do. But in most developing countries, the problem has been the converse, and arrangements for consultation have been inadequate.

THE ROLE OF THE LEGISLATURE

By virtue of its legislative authority, the parliament or congress may make or mar plan implementation. Since all plans invariably require some legislative action to empower the executive to carry out its policies, they must in some sense be reconciled with the political position of the legislature. But the particular procedures which may suitably be followed in order to fulfil this condition are bound to vary with the political situation and constitutional system prevailing in each country.

In most countries, parliament or congress has had no formal role in the preparation of the plan; the views of the legislature on the acceptability of the plan proposals have been ascertained by informal means. In France, however, as just noted, the plan outline indicating a number of alternatives or "options" has been submitted to Parliament and the preparation of the plan itself has been completed only after these "options" have been voted upon. And in India, comments on the plan outline have been prepared by Parliament after it has been considered in detail by a number of parliamentary committees.

Practice has similarly varied among countries in regard to the submission of the final plan document to the legislature. In some countries, medium-term plans have been submitted to the parliament or congress to be voted into law. Some have contended that such enactment raises the status of plans in the eyes of both political leaders and the public and that, moreover, in committing the executive to its implementation, it ensures continuity in the event of a change in government. On the other hand, no medium-term plan can set out all the specific steps to be taken for its implementation and its legislative enactment can at best only ensure in a general way that subsequent actions of the Government or legislature conform to the objectives of the plan.

A number of other countries, including France, India and Turkey have adopted a compromise solution by which the plan has been submitted to Parliament for discussion and approval as an instrument for guiding the Government's economic and social development policy.[1] However, many developing countries have not followed any formal procedures for submission of their plans; and these have simply been accepted as statements of the Government's economic and social policy. Experience, in fact, indicates that the formal status of a plan has had little effect on its execution. Ultimately, it is not the status of a plan but its political realism and the commitment of the Government to its execution which determine how effectively it is implemented.

PLANNING AND THE PRIVATE SECTOR

It has already been mentioned that, since a major part of the total output and investment of most developing countries lies within the private sector, only a qualified meaning can be attached to the implementation of comprehensive plans. This, however, in no way lessens the need to promote activity in the private sector in the desired directions. The very size of the sector has in fact led many planners to insist upon the importance of enlisting its active participation in the planning process. The machinery and the measures which some developing countries have employed to this end are the subject of a separate chapter. But, in the context of the present discussion, the nature of the relation of the private sector to the planning process may be briefly explored.

Assertions of the importance of the participation of the private sector in planning may sometimes represent no more than general expressions of hope that the community at large will strive more energetically and harmoniously towards the objectives of development. What is discussed here, however, is the more specific and concrete issue of the relation of private producers to the planning process since the power of decision which they wield over output and investment is clearly of immediate, and major, relevance for development policy.[2]

Where plan targets for output and investment have been expressed in very aggregative terms, the meaning of participation by the private sector in the planning process has likewise been of a very general nature. The main problem for government has been to create conditions conducive to the expansion of private activity, and this is a problem not uniquely related to planning. In some countries, however, the introduction of planning has given rise to additional difficulties because it has been identified by private producers with governmental interference inimical to their interests. In such a context, efforts to overcome the hostility of the private sector and to persuade producers that governmental and private action may be mutually supporting rather than conflicting, have been of major importance. To this end, some Governments have arranged for the representation of private groups on their high-level planning bodies; this has supplemented the use of the more established means for spreading understanding of their plans. However, participation of the private sector in the planning process, when interpreted in this general sense, is obviously no more than a part of the general problem, which confronts all Governments, of explaining and gaining political support for their policies. While the actual network of political and organizational relations between the central authorities and the private sector which has developed in individual countries is often very complex, it is part of the political fabric and need have no special association with planning.

Such consultations with the private sector, however, have also served another purpose more directly related to the planning of development policies. They have been a means through which the public authorities could obtain, and exchange information about, technical and economic conditions surrounding different activities. Such knowledge, which is in the nature of field research, is a prerequisite for the design of measures and, as discussed in a later section, has often failed to receive the attention it deserves. The ineptitude of governmental measures is the frequent complaint of private producers and it should be recognized that the lack of direct

[1] In France, for instance, the law relating to the adoption of the fifth plan (Law No. 65-1001 of 30 November 1965) is phrased as follows: "The 5th Plan... annexed to the present law is approved as a frame for the investment programmes for the period 1966-1970 and as an instrument for the orientation of economic expansion and social progress". (*Unofficial translation.*)

[2] This is not to ignore the fact that the private sector is also composed of many other economic and social groups, such as trade unions, or *rentiers*, whose responses to policy are important for development. While, for example, most development plans have centred their attention mainly on questions surrounding the level and composition of output and investment, the effect of plans and policies on income distribution may, if the attitudes of the various social groups have not been taken into account, bring failure in implementation. However, it has not been possible to deal with issues of this nature in the present chapter.

knowledge on the part of government officials not infrequently justifies their complaint.

More direct forms of participation in planning by the private sector, particularly the industrial sector, have, however, been advocated. The impression has gained ground that effective planning in mixed economies demands the elaboration of a comprehensive system of targets for output and investment of all the major branches of productive activity, and that, since many of these branches are under private control, a network of committees is needed in order to secure the participation of private producers in the formulation of targets and implementation of plans. This impression has acquired force from the example of planning in France where such a system of committees, covering most branches of activity, has functioned successfully for some time.

Several advantages have been claimed for such an extensive form of private participation. For one thing, consultations with the private sector about the targets and forecasts for private activity have been a valuable step towards formulation of a consistent plan.[3] A main advantage which observers have stressed, however, has been the role of the committees in inducing producers to act jointly in ways that will bring about attainment of plan targets. On the one hand, the plan has served as a kind of national market research survey, revealing to producers what the growth in demand for their output could be if its assumptions were realized; on the other hand, the committees have served as a means through which the confidence of producers in the feasibility of the plan could be strengthened. And the more individual producers could be persuaded to act in accordance with the plan—because they believe that other producers would do likewise—the more the assumptions of the plan about private producer behaviour would be translated into reality.

However, as members of the Commissariat du Plan have themselves pointed out, it is very doubtful whether the French system can be usefully transplanted to the conditions of a developing country. The system operates in conditions of a developed, industrial economy where habits of consultation among industrialists and with the central authorities have been long established. In origin, moreover, the purpose of the system was different from what might be expected in a developing country. As their name betokens, a principal aim of the modernization committees was to stimulate review of, and to promote innovation in, an industry which, before the war, had been highly protected and technologically backward; and, in view of the highly diversified nature of the economy, a fairly complex network of committees became necessary for this purpose.

In most developing countries, both the general economic conditions and the purposes of planning are quite different; and these suggest that arrangements for participation by the private sector should follow different lines. In most developing countries, industrial output is composed to a large extent of consumer goods and, while there may be an interest in restricting or preventing the production of luxury and semi-luxury products, the composition of the bulk of the output is not a matter which is of critical importance for planning. For the implementation of plans, two questions regarding output and investment in private consumer goods industry are important. The first is whether the total volume of final output expands according to the forecast; and on this score, the need for active participation of the private sector in planning takes the form, discussed above, of creating a climate of confidence among private producers and investors in the long-term prospects of the economy. The second is whether the lines of production which are initiated or expanded in the private sector are those which maximize output in relation to scarce productive resources, most notably, capital, skilled labour and foreign exchange. For this purpose, what is needed is not the active participation of the private sector in formulation of the plan but the establishment of guidelines by the central authorities to indicate the kinds of new activities which, because of their effects on scarce resources, will be favoured by such government measures as selective fiscal or credit policies or import and building licences.

This said, however, some qualifications must be immediately added. While little importance attaches to the relative proportions in which the increases take place in the output of such commodities as, say, bicycles, household utensils and furniture, this does not mean that no specific branches of production are of special interest. In undertaking development planning, a main purpose is the consideration of

[3] In the formulation of plans, the detailed elaboration of targets for output and investment in the private sector during the final year of the plan is usually undertaken on the ground that it improves the test of the plan's consistency. The preoccupation with the final-year consistency of a plan in developing countries has been criticized as misplaced since, in view of the great uncertainties which underlie both the estimates in plans and the course of actual events over the plan period, the likelihood of detailed plan targets being realized is very slight (see, for example, R. Vernon, "Comprehensive model-building in the planning process: The case of the less-developed economies", *The Economic Journal* (Cambridge), March 1966). This, however, does not take account of the fact that a principal reason for testing the consistency of a plan is to determine whether its priorities are correct. The most important question is not whether targets will be realized but whether the relative emphasis of policies among different sectors and branches of activities is such as to minimize the emergence of imbalances. However, the criticism is well taken in the sense that the detailed elaboration of targets embracing all branches of production is, for this purpose, probably not necessary in many developing countries. The exercise becomes useful only where the Government utilizes such policy measures as direct controls which are highly specific in effect.

trends and problems within a longer-term perspective, in order to identify actions which need to be taken now if future growth is not to be slowed down by the emergence of foreseeable shortages or difficulties. Viewed in this way, development planning is a continuing effort to take current decisions so as to correct for emergent or foreseeable imbalances. It is not so much planning for balanced growth as planning to lessen an unending succession of actual, emergent or foreseeable imbalances which arise as the consequence of growth.

But the areas of production in which imbalances are likely to emerge are precisely those in which the initiative of the private sector is often weakest. In the industrial sector, these areas embrace infrastructure projects and the industries producing capital or intermediate goods where capital costs are large, gestation periods lengthy and profitability uncertain. To these must be added food production in the agricultural sector, where the weight of traditional institutions and customs also smothers private initiative. And mention should also be made of the development of production for export, which is another area of weakness in many countries.

In most, though not all, developing countries, infrastructure projects are undertaken entirely within the public sector, and the question of the participation of private producers does not arise. In the production of capital and intermediate goods, however, some combination of roles by both the public and the private sectors is common; these range from coexistent public and private enterprises in the same industry, through different kinds of mixed ownership to exclusive private ownership supported by specially favourable governmental measures. And it is in such specific areas rather than throughout industry as a whole that the need exists for participation by private producers in the planning process. Programmes for specific industries in these areas must clearly be drawn up and implemented in close consultation with private producers.

In the food-producing sector, it is irrelevant to speak of private participation in similar terms. Composed as the sector usually is of a multiplicity of landowners and a large, illiterate peasantry functioning within a traditional system of social relations, the reform and modernization of the sector is a condition of meaningful participation. It is where a modern sector has been established that some form of participation through co-operatives or farmers' organizations has been most practicable.

The conclusion to which this discussion leads is that, given the stage of development and the purposes of planning in most developing countries, it is not generally necessary for effective planning to have a comprehensive set of targets for output and investment in the various branches of private activity, together with the participation of private producers in a comprehensive system of planning committees at the branch level. *Ad hoc* committees, however, for specific lines of production whose development is of long-run importance for the economy, may be very much needed. But the limited nature of direct participation at the level of specific branches of production in no way lessens the importance of efforts at the national level to broaden general support throughout the private sector for planned development.

ADMINISTRATIVE MACHINERY FOR PLANNING

While plans are political documents, they must initially be formulated and finally be implemented by governmental administrations. Even where the political commitment to planning has been assured, the problem facing most developing countries in welding together machinery for planning within government has by no means been inconsiderable. Administrative systems were generally established to fulfil functions much more limited than those demanded of present-day Governments, and administrations have not possessed the flexibility needed to carry out new and larger responsibilities efficiently. The over-centralization of authority, the concomitant lack of competent staff at the middle and lower levels and the consequent multiplication of cumbersome and time-wasting procedures have been among the major reasons for administrative rigidity. Further, the habit of interdepartmental co-ordination of activities, so necessary for planning, has been largely absent. Some observers have, in fact, singled out administrative inefficiency or limited administrative capacity as principal obstacles to the introduction of an effective planning process in many developing countries. This should not be understood to mean that the introduction of a functioning planning system is simply a matter of making suitable organizational arrangements within government. The effective establishment of such a system depends first and last on the political commitment to planned development. But it is true that the creation of an efficient organization is an important subsidiary task.

In discussions of the machinery for planning, much emphasis has sometimes been placed on the issue of the status and location of the central planning agency. This has been in recognition of the fact that, if planning is to become firmly rooted, the planning agency needs to be well established as a permanent institution of the governmental system. The status and location of the planning agency are, in fact, not merely an administrative question but are indicative of the importance attached, at the highest political level, to development planning. Where planning is being seriously attempted, it is essential, as described earlier, that the executive heads of government play a direct role in plan preparation. The executive heads must decide on the objectives and major policies of a plan, and since the central planning agency is responsible for the technical work underlying these decisions, it will necessarily be placed close to the centre of government.

In practice, the arrangements which most countries have chosen in establishing central planning agencies have comprised one of the three following kinds: the establishment of a planning unit within an existing administrative department such as the ministry of finance or economic affairs, the creation of a new planning ministry under a political head, or the establishment of an autonomous body with a governing body as well as a technical secretariat. A fourth variant adopted by some countries, such as Venezuela, has been to establish a technical secretariat under the direct authority of the chief executive.

There is no single arrangement that will suit all countries, and each particular variant raises its own political and administrative problems. But those developing countries with considerable planning experience have tended to favour the creation of an autonomous body closely linked to the executive. For the reasons suggested above, it is argued that the central planning agency needs to have easy access to the political authorities and to have the status within the governmental system that will enable it to obtain information from, and enter into discussions with, other government departments. It is also stressed that the autonomy of the planning agency is a guarantee of its impartiality in advising the executive on programmes and policies affecting individual ministries and agencies.

However, while the status and location of the central planning agency is not unimportant, it can hardly be stated too strongly that planning is a function which has to be carried out by the governmental administration as a whole. It cannot be adequately discharged without the full participation of the operating ministries and agencies. The planning agency has the task of advising on development policies and of promoting their co-ordination within the framework of the plan. But the operating ministries and agencies, being responsible for the preparation and execution of programmes and projects and for the administration of laws and regulations, are the media through which development policies are translated into action. In advising ministers on policies and in administering policy decisions, they have an essential role to play in both the formulation and the implementation of plans.

The problem of drawing the administrative departments and agencies into the planning process is partly a question of inducing them to develop their own machinery for planning. But, as just suggested, this often demands farther-reaching reform and modernization of administrative structures. This larger question cannot be dealt with in detail here, but it is worth noting that the introduction of planning can serve to give a forward impetus to such reform. While the central planning agency tends to be regarded at first with suspicion and resentment by the departments,[4] it can act as a catalyst in inducing them to apply the same disciplined approach to the planning and management of their activities as inspires the national plan. It has been the experience of many countries that the personal efforts of the head of the planning agency, and the development of a practice of informal consultation between the ministries and the planning agency, have often proved an important means of fostering a new attitude among the ministries and of bringing them more effectively into the planning process as active participants.

The participation of the ministries and agencies in plan formulation is needed both at the preliminary stage when a broad framework is being elaborated and at the later stage when programmes and projects for separate sectors and activities are being worked out. At the preliminary stage, as discussed earlier, the task of the central planning agency is to provide the executive with a general analysis of trends and possibilities that will enable the latter to take decisions on major policy issues. In the preparation of this analysis, the ministries can provide expert knowledge about problems or possibilities in their own areas of activity, thus not only verifying the judgements of the planning agency but also leaving it freer to perform its unique function of assessing the interrelations of the different sectors and activities.

Countries with substantial planning experience have generally evolved procedures to provide for such consultation at this stage of plan formulation; and these procedures have certain common features. At the ministerial level, co-operation has been formally established through the membership in the planning commission or in interministerial planning committees of the heads of departments responsible for developmental subjects. At the working level, the departments have usually been brought into the planning process when the planning agency has invited their comments on an early outline of the

[4] The early experience of Pakistan has been described as follows: "The (Planning) Board's requests for information or for the submission of proposals frequently encountered passive resistance which handicapped and delayed its work. When it began making suggestions for changing projects submitted by the various ministries, departments and agencies, apathy sometimes gave way to open hostility". Albert Waterston, *Development Planning, Lessons of Experience* (Baltimore, Johns Hopkins Press, 1965), p. 439.

plan. This has been the practice, for instance, in India, Pakistan, the United Arab Republic and Venezuela. At this point, the departmental staff has had an opportunity to examine the plan proposals as they affect activities within the jurisdiction of the department, to express their views on these proposals and to suggest changes. These comments and suggestions have been reviewed by the planning agency and taken into account in the further elaboration of the plan. A decision regarding the extent to which the plan outline should be modified in the light of these comments may be taken by the agency on the basis of the general guidelines it has been given, or it may have to be reached at a higher level.

In connexion with the preparation of the final draft of the plan-frame, sectoral or functional working parties or advisory panels which include senior government officials have sometimes also been established to assist the planning agency in its work. Alternatively, or in addition, representatives of the operating departments and others have been invited to participate in "round-table" discussions of specific aspects of the plan. Such discussions, for instance, have been an important regular feature of the process of plan formulation in France and Venezuela. They have been found valuable not only because of their substantive contribution to the formulation of the plan but also because of the opportunity which they afford for closer contacts among officials of the various departments and the planning agency.

Once the plan outline has been completed and approved, the plan enters its second stage when programmes and projects for the various sectors and activities have to be worked out. Plan preparation at this stage, when broad targets and guidelines are translated into specific programmes, rest very heavily on the work of the ministries and agencies. Commonly, however, in the initial attempts of countries to carry out development plans, this has proved to be the weakest link in the planning process. It has been observed with regard to experience in Pakistan that:

> "The fundamental weakness of the First and Second Plans has been that the planning was not built in depth; whereas an effort was made to develop consistent, aggregative planning frameworks, not enough effort went into filling these frameworks with well-conceived, well-engineered projects and programmes. This has had the double disadvantage of making planning somewhat theoretical and vague at the project level and creating difficulties in the way of offering an adequate portfolio of projects for purposes of foreign aid commitments."[5]

[5] Mahbub ul Haq, *The Strategy of Economic Planning: A Case Study of Pakistan* (Karachi, Oxford University Press, 1963).

This observation regarding the lack of concrete programmes could be applied to the early phases of planning experience in virtually all developing countries. And because the supply of suitable projects has been inadequate, the implementation of public development programmes has been impaired. While the consequence may sometimes have been that available resources have remained under-utilized, it should be noted that this has not necessarily been so. The more likely outcome has been that the resources intended for the public development programmes have been absorbed by unplanned increases in private or social consumption or in private investment. In other words, the actual level and composition of total investment has turned out to be different from that which was intended or planned. The whole quality of the development effort has been adversely affected, not because resources have been inadequate, but because they have been under-utilized or misallocated.

Faced with the inability of particular ministries or agencies to generate a sufficient supply of projects, countries have resorted to various measures to overcome the problem. In some countries, central planning agencies have sought to compensate for the weakness of individual ministries by directly undertaking the preparation of projects themselves. Others have established committees of professional and business men with technical and local expertise whose function has been to act as a source of ideas for possible projects. Yet others have introduced special programmes to enlarge the supply of projects; Pakistan, for example, carried out a "crash programme" under which a large number of feasibility studies were completed by domestic and foreign technicians in order to build the stock of projects available for execution in the latter part of its second plan and during its third plan.

But it is recognized that as a longer-term solution, the emphasis needs to be upon the creation of planning units within the various ministries and agencies, these units being charged with the preparation of programmes and projects on a continuing basis. What has often hampered the establishment of effective units has been the lack of personnel with the skill and training to prepare and appraise potential projects. Foreign technical assistance has been helpful in easing this problem, but the primary need has been for the extensive training of national personnel.

Many developing countries have recently been attaching much greater importance to this aspect of planning and they have been taking steps to strengthen their resources for such work. However, the considerable emphasis which has been given in the past few years to the need for careful preparation and appraisal of individual investment projects should not be allowed to obscure the fact that the task of elaborating more effective programmes for different sectors and branches of the economy has broader ramifications. While the systematic preparation of feasibility studies for a sufficient number of individual investment proposals is an essential step in the elaboration of programmes, it is not the only step. It has to be preceded by the initial identification of possible projects which would appear to respond best to actual needs or to take fullest advantage of existing opportunities. Further, the individual investment projects proposed for implementation within a sector should be considered both in relation to each other and in relation to other measures as components of a coherent programme for the sector. In other words, the elaboration of a sectoral programme does not begin and end with the preparation and appraisal of individual projects; it begins with research into the development problems and possibilities of the sector and ends with a programme not only of individual projects but also of other measures which together best meet these problems and possibilities.

This criticism may appear to be a counsel of perfection. It is advanced, however, not as an argument for formally more complete planning but to stress the importance of research as a determinant of the quality and effectiveness of development programmes. The effectiveness of the projects proposed for implementation, no matter how carefully prepared and appraised, can be no better than the skill and knowledge which is applied to the preliminary identification of possible projects; in other words, it can be no better than the technical, economic and social research which is undertaken to reveal new opportunities and to define the steps needed to overcome existing problems. It is through such research that the specific objectives to be pursued in individual sectors can be clarified and that, moreover, the need for programmes of interdependent projects and measures can be more readily appreciated.

The experience of developing countries in attempting to plan the expansion of agricultural output perhaps provides the most obvious evidence in support of this criticism. Development plans have generally called for an acceleration in the growth of agricultural output and various measures, including public investments, have been utilized to promote this aim. But actual performance has commonly fallen substantially short of the expectations embodied in plans, and the effectiveness of the various measures has repeatedly been called into question. The fact, however, is that the measures and investment projects actually carried out have often been chosen on the basis of scant knowledge about the physical and institutional conditions determining the behaviour of producers. The selection of measures and projects has been guided more by broad preconceptions about the requirements for increased output than by objective identification of the specific obstacles or limitations to expanded output which prevail in the various agricultural areas of the economy. This no doubt helps to account for the piecemeal nature of many of the projects and measures which have been implemented. Most certainly, the obstacles to the expansion of output have sometimes been of an institutional nature rather than of a simply technical or economic character, and the main difficulty has been political resistance to institutional reform. But even where such reform has been a possibility this alone has not been a solution to the raising of output, and the need for more coordinated programmes based on more systematic research and analysis has been apparent.

While the lack is generally evident in agriculture, it is true that the case for more thorough research by government as a precondition for more effective planning does not apply with equal force to all other sectors. It is strongest in those areas, such as agriculture or transport, in which the innovatory role of the public sector is usually very large. It is apparent, too, that the kind of research required differs among sectors; the information and analysis needed for elaboration of a long-term educational programme is, for instance, of quite a different nature from that called for in the commodity sectors.

But these considerations do not alter the general point. Although it is at the sectoral level that some major problems of development must be solved, the resources and machinery for planning at this level have commonly been the weakest element in the planning process of most countries. Much of the talent and expertise available for planning has been absorbed by the central planning agencies in the preparation of comprehensive national plans, and the planning units within the operating ministries have been poorly staffed. More broadly, the ministries have remained rooted in their traditional functions and have lacked the new cadres of trained staff and the organizational flexibility to undertake the research and planning necessary for the initiation of new development policies and programmes. It seems true that a more partial approach to planning, in which attention was concentrated on certain sectors and branches of activity of strategic importance for development, could yield greater results to overall progress in many countries. And if this is true, it means that much higher priority should be given to the reform and strengthening of the operating ministries.

REGIONAL AND NATIONAL PLANNING[6]

Governments in developing, as well as in developed, countries have become increasingly concerned about the growing concentration of enterprise and populations in certain regions and urban areas while activity in other regions has stagnated or declined. The problem of regional development planning has therefore received much attention in recent years. Various regional and local authorities have established planning organs to deal with specific problems of their localities, but these bodies have tended to pursue their activities without reference to each other or to the national planning agency. A few countries have also attempted to set up a network of planning organs at various levels of government, but an effective division of labour and co-ordination of efforts among these bodies has generally proved difficult to achieve. Moreover, owing to the paucity of regional economic data and the shortage of qualified personnel, the scope and quality of regional plans has generally been inferior to that of the national plans. This has prevented an effective "regionalization" of national development plans.

The construction of regional plans within the framework of a national plan involves more than the territorial disaggregation of the latter. It requires that the national plan itself be formulated with regional development objectives in view. To this end it is necessary to appraise the feasibility and implications for national development of various approaches to regional development and to specify options as regards the concentration of development efforts in particular regions. Developing countries, and even many developed countries, do not possess adequate economic data for territorial subdivisions to undertake such analyses. The collection of data and the study of regional economies is therefore an essential first step towards improved regional development planning. This has been attempted, for instance, in the United Arab Republic where the planning agency for the Aswan region has undertaken extensive resource surveys, feasibility studies for mining and industrial projects and other research, on the basis of which a comprehensive plan for the region as a whole has been prepared. In France, likewise, a number of regional economic surveys have been undertaken with a view to intensifying regional planning activities and strengthening the regional dimension of the national plan.

The main organizational problem in regional planning relates to the establishment of an effective division of labour between the central planning agency and the regional planning bodies. The obstacles to be overcome in this connexion are generally of two main kinds: conflicts of jurisdiction between planning organs established by national and regional or local authorities, and the technical inadequacy of many subnational bodies responsible for planning. To these might be added a third obstacle, which is found especially in countries where administration is highly centralized, namely, the reluctance of authorities in administrative subdivisions of the country to assume planning responsibilities.

An effective division of labour would require that the outline of the regional plan be prepared by the central agency in conjunction with the national plan and in consultation with regional bodies. That outline would form the basis for the elaboration of detailed programmes which could best be undertaken by the regional planning units in the light of their knowledge of regional conditions and needs. Regional programmes would subsequently be reviewed at the centre, by the planning agency and by the administrative departments competent in the various fields covered by the regional programme. The implementation of specifically regional projects and programmes would then be undertaken as far as practicable by the regional authorities.

The first and perhaps most crucial step in this process, namely, the formulation of a plan outline for regions by the central agency may be difficult to achieve where regional and central planning organs are responsible to different levels of government. In certain countries with a federal system of government, the preparation of regional plans is within the competence of state governments; and there is a major problem of co-ordinating state and national plans. Only a few countries have so far developed institutional arrangements through which a certain measure of co-ordination has been achieved. In India, for instance, the outlines of state plans are prepared by state planning organs concurrently with the national plan, and it is only after their completion that they are reviewed and co-ordinated by the Central Government's Planning Commission in consultation with the state governments. In the case of Pakistan, the problem of a possible jurisdictional conflict between provincial and national planning authorities did not arise because representatives of the two provincial governments are members of the (central) Planning Commission which formulates the national plan in the light of regional requirements. In countries where government is highly centralized, as for instance in France, the central planning agency usually has jurisdiction over the planning units in the administrative subdivisions of the country. Responsibility for initiating the formu-

[6] Regional planning in the sense of multinational planning is another aspect of implementation which is of growing importance for many countries. It has not, however, been possible to discuss this aspect in the present study.

lation of regional plans therefore rests with the central planning organ.

The preparation of detailed programmes by the regional organs is often handicapped by the lack of qualified staff to prepare programmes efficiently and with dispatch. The scarcity of trained personnel tends to be even more severe in the case of regional planning units than in central administrative departments because of the reluctance of people with the needed qualifications to accept appointments outside the major urban centres. In these circumstances the central agency may be obliged to intervene extensively in the preparation of regional programmes either by centralizing much of the regional planning work at headquarters or by seconding staff to the regional planning bodies. An alternative solution, namely, the physical location of regional planning units at the seat of the central government, which has been occasionally adopted as a temporary expedient, for instance, in Venezuela, where the Corporación Venezolana de Guayana was established with temporary headquarters at Caracas, is unsatisfactory because it removes the regional agency from close contact with local conditions and institutions.

Whatever specific arrangements may be made for the elaboration of regional programmes and projects, regional bodies should be encouraged to participate to the greatest possible extent. The successful implementation of regional programmes depends in very large measure on the interest and co-operation of the inhabitants of the region. This has been found to be true even in regions of new settlement where programmes prepared by "outsiders" have occasionally met with resistance even from settlers who have recently moved to the region.

While the weakness of regional planning organs has hampered the establishment of effective regional planning procedures, the assumption of regional planning responsibilities by the central planning organ does not provide a satisfactory solution to the problem in the long run. It should be considered as a temporary expedient while the planning units at the regional level are being built up. The central agency's role should eventually become primarily that of initiator and co-ordinator. The effective performance of that role is, however, of particular importance in view of the geographic dispersion of regional planning activities. A clear definition of the respective function of the central and regional organs is therefore necessary and the co-operation between these bodies should be given an institutional framework. At the same time regional authorities should be as far as possible associated with the formulation of the national plan so that their objectives and needs as well as their experience may be adequately taken into account.

SUMMARY

The first and foremost condition for the implementation of a development plan is the political will to pursue effective policies. While political realism is essential in drawing up a plan, an excessive preoccupation on the part of planners with the need to conform the plan with "present political realities" may defeat its purpose of promoting development. Political judgement has to be exercised in devising a compromise between policies desirable for development and politically feasible actions.

The limitations on the implementation of comprehensive plans in mixed economies should be recognized. Since a major part of output and investment is subject to private decisions, many of the quantified changes set forth in plans are not within the power of Governments to realize. These changes have often been too readily identified as targets, whereas their purpose is rather to guide policy decisions.

Plan implementation begins at the stage of plan preparation when decisions are taken on major policy issues. It continues at subsequent stages when successively more specific decisions are taken on more disaggregated measures and actions. At each stage some planning precedes decision taking. The planning process is thus part of the decision-making process at every level of government.

The executive heads of governments have to participate in the planning process from its very beginning when the major objectives and lines of policy are determined. In many countries formal, institutional arrangements have been established through the creation of bodies headed by the prime minister or chief of state, which have had general responsibility for planning. However, formal procedures have not necessarily proved more effective than more informal arrangements; it is the will and ability of the executive to carry out effective development policies that count.

Since plans normally require some legislative action to empower the executive to carry out its policies, they need to be reconciled with the political position of the legislature. Procedures to ensure the plan's acceptability to the legislature are bound to vary with the political situation and constitutional system prevailing in each country as well as with the specific legislative provisions establishing the planning machinery. What is important is that these be sufficient to ensure that the legislative requirements of the plan will be fulfilled.

Resistance by the private sector to the plan may obviously weaken its political foundation. To gain broad support, some Governments have arranged for the representation of private groups on high-level planning bodies in addition to employing the usual means for publicizing and explaining their plans.

In view of the power of decision which private producers wield over output and investment, more direct and specific forms of participation in plan formulation, particularly by private industry, have also been advocated. A network of mixed committees for particular industries and branches of production appears to have been successful in certain developed countries, but it is doubtful whether the general application of such an arrangement is either practical or necessary in most developing countries. Close consultation between government and private producers, however, is indispensable in branches of production of strategic importance for growth.

Planning is a function which has to be carried out by the governmental administration as a whole. It therefore requires not only the creation of a central planning agency close to the centre of government but also arrangements to ensure the full participation of operating ministries and agencies in the planning process. The problem of drawing the administrative department and agencies into the planning process, however, has generally not yielded easily to solution. Apart from the establishment of some planning machinery within individual ministries and agencies, it has demanded difficult changes in traditional administrative attitudes and procedures.

In early attempts to introduce development planning, the preparation of programmes and projects within sectors by the ministries and agencies has generally been the weakest link in the planning process. The most obvious symptom has been shortages in the supply of well-prepared projects. But, in addition, insufficient analysis and information concerning problems and possibilities in individual sectors have limited the quality and effectiveness of proposed programmes both for investment and for other measures. While central planning agencies have sometimes been obliged to assume responsibility for the preparation of projects, the longer-term solution has been to strengthen the capacity of ministries and agencies, not only to prepare projects but also to draw up co-ordinated programmes on the basis of more thorough economic and technical research.

Regional development planning has suffered from similar, as well as other, weaknesses. Efforts to build up suitable machinery and procedures have encountered such difficulties as a lack of adequate regional economic data and trained personnel as well as administrative obstacles to the establishment of an effective division of labour among organs at the various levels of government. Attempts to plan regional development from the centre have also been hampered by a lack of familiarity with local conditions and by the resistance of local populations. It is generally agreed, however, that regional development objectives need to be given greater weight in the formulation of national plans and that regional organs need to be strengthened so that responsibility for the formulation of detailed regional plans may be decentralized.

Chapter II

THE ROLE OF THE FISCAL BUDGET IN PLAN IMPLEMENTATION

In this chapter, some of the experience and problems of developing countries in the use of the fiscal budget as a principal instrument of plan implementation are discussed. Since the role of the fiscal budget is complex, its relation to planning has to be viewed from several standpoints. Through its responsibility for the preparation and control of the annual budget, the ministry of finance has customarily been the primary agency concerned both with the conduct of fiscal, budgetary and other policies for the short-term economic management of the economy and with the annual programming of public expenditure. These, however, are activities which are central to the implementation of medium-term plans. Though it is an aspect of development planning which has generally received insufficient attention, the effective implementation of plans depends in no small part upon the skill with which they are accommodated to short-term changes in circumstances. At the same time, programmes for public expenditure, which have commonly constituted the core of the medium-term plans drawn up by most developing countries, have necessarily been executed through the annual budget. The programmes for public expenditure contained in medium-term plans, however, have usually excluded current expenditure from their detailed consideration, although the effective control and rationalization of current expenditure have been a condition of plan implementation. Finally, the fiscal budget has also been closely linked with planning in its role as a principal means for increasing the proportion of resources allocated to developmental purposes.

These several aspects of the relation between planning and the fiscal budget—namely, annual planning, the programming and execution of public development expenditure, the control and rationalization of current expenditure, and the mobilization of domestic resources for public sector programmes—are separately discussed in the following sections.

Annual planning and the fiscal budget

The disaggregation of the public development programme proposed in the medium-term plan into a series of shorter-term action programmes is usually considered to be one element of annual planning; and some of the problems which arise on this score are discussed in the next section. But before the composition of expenditure can be considered, the resources likely to become available for implementation of the annual programme have to be determined; and it is this larger aspect of annual planning which is dealt with here. Besides the programming of expenditure, annual planning is concerned with a more difficult, and continuing problem which faces all countries in the execution of medium-term plans: this is the flexible management of budgetary and other short-term policies so as to minimize the adverse effects of changing circumstances on the progress of implementation.

An annual plan has been widely identified as a national economic budget for a period of one year—an economic counterpart of the customary fiscal budget. In the developed market economies, national economic budgeting, though not usually linked explicitly to a specified time period, has been a familiar feature of economic management for some years. For the periodic determination and revision of fiscal, budgetary and other short-term policies, it has become customary to make estimates of the prospective trends in aggregate demand and its major components, in production and imports and in such other principal economic variables as employment, wages and prices. Such work, however, has not required any planning machinery as usually understood, though an economic agency or unit has normally been established within the governmental system for this purpose.

In most developing countries, some form of national economic budgeting, though necessarily in a much cruder and more incomplete state, has similarly been attempted; this has usually devolved upon the economic staffs of ministries of finance or central banks. However, the requisite character of national economic budgeting or annual planning in most developing countries differs in some important respects from that in most developed market economies; and there is stronger need for an active role by the planning agency in such work.

In developed market economies, the analysis required for short-term policy decisions is largely concerned with highly aggregated demand-supply balances for the economy as a whole. It is taken for granted that demand-supply balance in markets for specific commodities or productive resources will be secured through changes in relative prices or through foreign trade. But in most developing countries, the greater inflexibility of their productive structures together with the scarcity of foreign exchange supplies makes such an assumption untenable for their economies. To assess whether a tolerable over-all equilibrium will be maintained, it is necessary to estimate not only the likely demand-supply balance at the aggregative level but also the likely balance in markets for critical commodities and productive resources. The well-known short-run instability in domestic agricultural production and export earnings which faces most developing countries only accentuates the importance of estimating these specific demand-supply balances.[1]

Failure to make forward estimates of specific demand-supply balances in order to guide short-term policy decisions often gives rise to avoidable short-run difficulties in the implementation of plans. The planned annual investment programme, for instance, has sometimes proved impossible to carry out because it has presupposed a greater expansion in the capacity of the domestic construction industry than the supply of trained manpower would allow. The capacity of the transport industry has similarly been frequently overlooked as an element limiting the feasible increase in total domestic activity. But perhaps the most common source of difficulty has been the emergence of unanticipated shortages in imported supplies of key commodities; the most typical, and obvious, instance is one in which supplies of imported equipment and materials have fallen short of requirements for the annual investment programme.[2] When such bottle-necks have arisen, the stock of unfinished projects has tended to increase and, unless very prompt action has been taken to restrict investment expenditure, inflationary pressure has been intensified. While some Governments, when faced with an impending foreign exchange crisis or rising domestic prices, have revised their scale of priorities, others have simply made across-the-board cuts in the development expenditures of the different ministries without regard to the distortions in priorities produced by these cuts. Moreover, while certain countries have made some estimates of the import requirements of their investment programmes, they have tended to neglect import requirements for the maintenance of current output; consequently, when supplies have fallen short of requirements, these countries have found themselves in the paradoxical, and inflationary, situation of adding to productive capacity in some industries while existing capacity has been forced to lie idle.

Of course, no matter how carefully annual programmes are assessed for consistency, dislocations in domestic activity cannot readily be avoided if the reductions in supplies of key commodities or resources assume sizable proportions. Even in countries with fairly well-established planning processes, the capacity to modify plans in order to accommodate changes in the level of supply of key resources is quite limited. This has recently been demonstrated by several instances among developing countries in which medium-term plans have either been postponed or abandoned because of large changes in such supplies. It is in order to lessen such disruption to orderly development that recent proposals for some more effective international machinery for compensatory financing have been advanced.[3]

None the less, the actual stage of annual planning, and the actual contribution of planning agencies, leave much to be desired in the vast majority of developing countries. It is true that there have been a few exceptions. In Turkey, for example, the State Planning Organization has annually prepared a fairly comprehensive framework of estimates of production, investment, exports and imports as a guide in assessing the consistency of short-term plans and policies. Surveys, for example, have been made of investment plans in the private sector in order to assess the level of public investment which would be consistent with the maintenance of aggregate demand-supply balance. And, while estimates of import requirements for specific commodities have been made

[1] An illustration of the general point made in this paragraph, which is interesting because it straddles both of the situations mentioned, can be drawn from the post-war history of French planning. In preparation of the earlier French plans, a system of physical balances was employed to compare likely requirements and supplies of real resources. But in the last several years, the French economy has become progressively more open as commercial policies have been gradually modified to conform with the aim of integration within the European Common Market. With the much greater openness of the economy and the self-imposed limitations on measures for the control of foreign trade, the attention of planners has shifted to the maintenance of price stability and aggregate, demand-supply balance; and the construction of specific, physical balances has given way in importance to the preparation of financial balances. This illustration refers to medium-term planning, but the logic is no less applicable to annual planning.

[2] While this situation is usually identified with a shortage of foreign exchange supplies, it should be pointed out that it can also arise for other reasons. When the countries supplying the equipment and materials are experiencing very high levels of domestic activity, there is a tendency for delivery periods to lengthen, and if no account is taken of the increased time-lag between orders and deliveries, the importing country finds that projects cannot be begun as scheduled. In such a situation it not infrequently happens that foreign exchange originally earmarked for investment goods is diverted into financing the importation of consumer goods which have shorter delivery schedules.

[3] See, for example, International Bank for Reconstruction and Development, *Supplementary Financial Measures* (Washington, D.C., December 1965). For an account of earlier work by the United Nations on this subject, see *International Compensation for Fluctuations in Commodity Trade* (United Nations publication, Sales No.: 61.II.D.3).

only for a few key products, such as petroleum, broader estimates of production and imports by sectors and branches of activity have been attempted in order to construct a balance for the external sector.

It is true, of course, that many developing countries have been in the practice of constructing foreign exchange budgets, either annually or at more frequent intervals, as a guide in the allocation of foreign exchange and import licenses. Such budgeting, however, has not generally served as an integral part of over-all annual planning. Certainly, the estimates regarding the prospective foreign exchange position which have been made in construction of the foreign exchange budget have often influenced decisions relating to short-term domestic policies, particularly monetary policy. But evaluation of the consistency between the foreign exchange budget and domestic production and investment plans and forecasts has not been systematically attempted.

Undoubtedly, planning agencies in many countries have also, in some degree, attempted to assess total resources and requirements on an annual basis. But in general, it is fair to say that, in so far as planning agencies have exercised a role in assessing the consistency of short-term policies, it has usually been effectively confined to evaluation of financial balance within the public sector. In Pakistan, for example, the Planning Commission appears to have played an important role in annual planning in co-operation with the Ministry of Finance. This, however, appears to have consisted largely in the preparation of separate estimates of the resources which might be made available during the coming year for the public development programme. The Planning Commission and the Ministry of Finance have then discussed and compared their separate estimates, the final decision on the size of the annual development programme being taken by the National Economic Council with the aid of their advice. In India, the Planning Commission appears to have played a somewhat similar role. It is notable, however, that in the draft outline of the fourth five-year plan, considerable emphasis was placed on the need for strengthening the annual planning exercise. Although India is a country with many years of planning experience, it was stated in the draft outline that "it has not been possible yet to prepare systematic annual balances and forecasts for key materials or to link up estimates of requirements adequately with plans drawn up for the more important industries, projects and programmes".[4]

Certainly, the difficulties confronting developing countries in assessing the consistency of short-term policies are not to be underrated. A major obstacle is the lack of statistical information for the analysis and appraisal of economic trends.[5] Data on current activities are deficient or are subject to lengthy time-lags in collection, and little is known about intentions in the private sector. In many countries, moreover, even current and proposed activities in the public sector as a whole are poorly known. Budget statements are often not comprehensive since they fail to report on the financial activities of autonomous agencies or public enterprises, and traditional systems of budgetary classification are of severely limited value for economic analysis. Further, very few countries have developed adequate systems for the control and appraisal of progress in the implementation of public development programmes.[6]

No general prescription can be made for the kinds and number of specific balances which are relevant for short-term policy decisions in developing countries; these are bound to vary with the individual circumstances of each country and, in particular, with such factors as the degree of openness of the economy, its stage of development and the policy instruments at the disposal of the Government. But the frequency with which bottle-necks arise in most countries does suggest that greater attention to specific balances as tools for the exercise of policy measures could improve short-term management of the economy.

PROGRAMMING AND EXECUTION OF ANNUAL DEVELOPMENT EXPENDITURE

Programming expenditure

In traditional practice, the primary concern of the ministry of finance in the preparation of the annual budget has been with the question of the financing of public expenditure. The programme of annual budgetary expenditure has been constructed in a routine way through compilation of the requests for allotments submitted by the various ministries and public agencies. The task of the ministry of finance has been to limit the annual increase in these requests in order to preserve some financial balance between total receipts and expenditure. In this way, the ministry has usually assumed a role in determining the composition of the annual expenditure programme, though the extent of this role has varied

[4] Government of India, Planning Commission, *Fourth Five-Year Plan—A Draft Outline* (New Delhi, 1966), p. 156.

[5] There is also an inherent difficulty in annual planning that does not arise from lack of data but from the fact that the plan has to be constructed some time before the end of the preceding period.

[6] For further discussion of the relationship between planning and government budgeting and of tecniques of budgetary classification, see the following United Nations publications: *Government Budgeting and Economic Planning in Developing Countries* (Sales No.: 67.XVI.1), *A Manual for the Classification of Government Transactions by Economic and Functional Categories* (Sales No.: 58.XVI.2), and *A Manual for Programme and Performance Budgeting* (Sales No.: 66.XVI.1).

widely among countries. In some countries, it has been no more than a broad determination of the total amount of financial resources to be allocated to each executing ministry; some arbitrary limit has been set to the annual increase in financial resources allocated to each ministry. In other countries, the ministry of finance has scrutinized in some detail the requests of the executing ministries, particularly as regards proposals for new projects or schemes. The question of the "desirability" of projects and schemes has thus been introduced into the discussions between the ministry of finance and the other ministries.

When medium-term plans have been drawn up, the programming of annual budgetary expenditure has obviously become a matter of particular importance for plan implementation. Indeed, it may be said that, in most developing countries, one of the initial functions of planning has been to bring greater order and coherence into public expenditure programmes. This means that some arrangements have had to be devised to ensure that projects and schemes included in the annual budget should be consistent with the public expenditure programme outlined in the medium-term plan.

Many countries have experimented with administrative reforms towards this end, but the problem is frequently far from having been solved. Ministries of finance have everywhere been reluctant to yield or share their power of decision over items of public expenditure; and, where there has not been strong support for planning at the highest political level, attempted reforms have often served more to breed mutual hostility and jealousy among government departments than to alter actual budgetary practices.

The problem, however, cannot be simply construed as a transfer of functions from one agency to another, though protagonists in interministerial disputes often pose it exclusively in these terms. Whatever the administrative reforms, provision has to be made for continuing execution of the central functions of the ministry of finance. Customarily, the ministry of finance has been responsible for ensuring both that all items of public expenditure are made in accordance with the financial regulations of the country and can be accounted for, and that ministries conform with the general prescription to observe reasonable economy in expenditure. In view of the importance both of preventing corruption in the public services and of economizing in the use of scarce resources, these functions of public accounting and of cost minimization are certainly not of negligible importance. Thus, the problem is not to discard established functions but to adapt procedures in order to accommodate the new functions.

Various countries have introduced different administrative changes in order to reconcile budgetary programming with these more traditional functions. In some countries, authority for approval of projects and schemes proposed for inclusion in the budget has been allowed to remain with the ministry of finance, the medium-term plan being accepted as no more than a general frame within which the executing ministries have drawn up their annual programme in consultation with the ministry of finance. In most countries, however, ministries of finance, being preoccupied with the control and limitation of annual, public expenditure, have lacked the broader outlook necessary for development planning; and consequently some more direct organizational link between the plan and the budget has been required.

A radical solution, which has been adopted in some countries, has been the assignment to the planning agency of exclusive responsibility for preparation of the annual capital budget. This certainly simplifies the task of ensuring that investment projects approved for inclusion in the budget are consistent with the medium-term plan. But it places a heavy administrative burden on the planning agency since the agency becomes responsible not only for thorough scrutiny of the financial as well as the economic aspects of each investment proposal but also for detailed preparation of the annual capital budget estimates; with this task to fulfil each year, the agency may have little time left for the broader advisory and technical functions which are its unique responsibility. A further objection to this solution is that it separates consideration of capital expenditure from that of current expenditure. Since the development programmes of some operating ministries entail both current and capital expenditures, this means that these programmes are not considered as a whole. Moreover, the division of responsibility for capital and current expenditure may accentuate neglect of the fact that some forms of capital expenditure generate requirements for higher levels of future current expenditure.

An alternative solution has been to request the ministry of finance not to include any projects or schemes in the budget which have not received the prior approval of the planning agency. This procedure incorporates the programming function into budget preparation without transferring any of the customary responsibilities of the ministry of finance to another agency. It does, however, give rise to a system of dual appraisal which has been widely criticized as being both cumbersome and time-wasting. Operating ministries have been required to prepare their project proposals in different ways for submission to two separate agencies. The planning agency has required information which would enable it to make a broad evaluation of the economic costs and benefits in the context of the medium-term plan. But when projects approved by the agency have later been submitted to the ministry of finance, a more detailed financial statement of costs has been demanded for the preparation of budget estimates and in order to satisfy the ministry that due attention has been paid to economy. In practice, moreover, this procedure has tended to discourage the development of a system of thorough project appraisal by the planning agency. Ministries have tended to seek the approval of the planning agency at a preliminary stage of project preparation, and only after receiving such approval have they prepared more careful and detailed estimates of costs for the ministry of finance. But this has reacted adversely on the quality of project appraisal by the planning agency and has provoked the—sometimes legitimate—criticism by the ministry of finance that the agency has approved projects without adequate evaluation of costs and benefits.

In those countries with some years of planning experience, the trend in administrative changes has been to work towards some form of joint and simultaneous scrutiny of budgetary proposals by the planning agency and the ministry of finance. The aim, in other words, has been neither to exclude the ministry of finance from budgetary preparation nor to duplicate its work in another agency; it has been to bring together the various agencies involved in budget preparation through the creation of common machinery.

In the paragraphs which follow, a brief description is given of the machinery established in some of these countries. First, however, it should be noted that the planning agency has usually participated in the scrutiny only of those proposals for budgetary expenditure which are considered to be of a developmental nature. These have been mainly items of capital expenditure, but they have included some items of current expenditure, such as those incurred by developmental schemes in the agricultural sector. This division of budgetary expenditures into developmental and non-developmental, which has perhaps been made best known by its utilization in the plans of India and Pakistan, has been criticized as an arbitrary form of classification. Almost any expenditure can be defended as developmental in some sense, and at no point can a clear line of division be drawn. But, regardless of its logical weakness, the classification has represented some improvement over previous practices. It gets away from the more usual identification of development expenditure with the capital budget alone and is thus a superior instrument for development planning. Moreover, in so far as it excludes items of expenditure which must anyway be decided on non-economic grounds, such as expenditure on defence or on law and order, it does no harm to the planning process. The main criticism which can be levelled against the classification is that it is usually not broad enough. Many items of recurrent expenditure, such as those on education, remain outside the planning process; and although, as discussed elsewhere, they have implications for development, these items may not be subject to the same careful scrutiny and appraisal as are components of the development budget.

Pakistan offers an example of machinery through which the planning agency, the ministry of finance and the operating ministries all participate in programming the development budget. In each of the two provinces of the country, a provincial development working party has been organized by the provincial governments, and these working parties undertake technical scrutiny of the development projects and schemes proposed by the various ministries or public agencies. After a project has been approved by either of these working parties, it is submitted to the Central Development Working Party if it is beyond a prescribed financial limit. This central working party is chaired by the Secretary of the Planning Commission and its members consist of representatives of the sponsoring ministries and the Ministry of Finance. Once this working party has approved a project, it submits its recommendations for decision by the Executive Committee of the National Economic Council, a committee which is presided over by the Minister of Finance.

In India, a comparable system has been gradually developed for co-ordination of the activities of the Planning Commission and the Ministry of Finance. Briefly, prior to the preparation of the budget, the Planning Commission initiates discussions with the various ministries about their annual plans and proposed budgetary expenditures. These proposals are submitted both to the Planning Commission for inclusion in the annual plan and to the Ministry of Finance. The Ministry of Finance, after reviewing them in consultation with the Planning Commission, submits them—as the programme of each ministry—to the Cabinet.

Again, in Venezuela, where the technique of programme budgeting has been extensively developed since 1962, a programme budget is prepared simultaneously with the more customary administrative budget. Proposals by the various ministries, prepared in the form of programme budgets, are presented simultaneously to the planning agency and the Ministry of Finance; and these two bodies jointly draw up the annual budget for submission to the Cabinet.

It is not to be claimed, of course, that even in these countries the work of programming the annual development budget has always proceeded smoothly. In a recent report on Pakistan, it was noted that "difficulties arise in the close integration of planning and budgeting because the two processes are carried out by separate organizational units and consequently by different groups of persons with different backgrounds, experience and skills".[7] Still, while administrative changes do not necessarily assure the effective programming of the budget, some such changes are clearly a necessary condition.

The specific organizational changes which are made to integrate planning and budgeting are bound to vary from country to country. But the experience of those countries in which planning has been practised for some years does at least suggest that these changes should be directed not towards the circumvention of the ministry of finance or the reallocation of some of its functions to a separate and independent agency but towards the fusion of its work with the functions of the planning agency and the executing ministries through the creation of common machinery.

Execution of annual development programmes

Co-ordination of the work of the planning agency, the ministry of finance and the other ministries in the preparation of the annual development budget is a major step towards effective planning. Much of the value of this work may be dissipated, however, if construction of the proposed projects or initiation of the proposed schemes is not carried out as planned. Substantial delays in the execution of annual programmes are, in fact, a common experience and they considerably impair efficiency in the implementation of over-all plans. The number of uncompleted projects accumulates, or projects that are completed cannot be brought into operation because related projects are not finished on schedule.

Statistical information on the extent of such delays is naturally scanty, though it is a frequent, if unconfirmed, impression that the volume of capital tied up in uncompleted or inoperative projects tends to increase more rapidly than new investment. However, an interesting illustration of how substantial these delays can be is provided by the data shown in table 1. These data happen to refer to projects within the private sector but they can be taken as exemplifying a general problem.

Sometimes the causes of delay lie in events beyond the control of the Government as well as of the individual enterprise. They may originate, for example, in a shortfall in imported supplies occasioned by an unforeseeable decline in foreign exchange receipts or by unexpectedly protracted negotiations for foreign aid. But they also commonly have their source in deficiencies in the planning and management of project execution.

The kinds of delays occasioned by such deficiencies are familiar, and are common to many countries. Projects have been approved for inclusion in the annual programme before detailed technical plans have been worked out or before the availability of the physical resources required for construction of the projects has been verified. Initiation of construction has been delayed because such advance work as the purchase of land sites or the negotiation of contracts has not been completed or because the release of funds for projects has been subject to cumbersome administrative procedures. In the stage of construction, poor scheduling of the various ac-

[7] "Experience of Pakistan relating to the interconnexions between budgetary and planning processes" (E/CN.11/BRW.4/L.13 and Add.1).

Table 1. India: Delays in implementation of a sample of investment projects in the private sector[a]

Length of delay	Number of projects at different stages of implementation			Total
	Projects completed	Projects currently under construction	Projects currently in planning stage	
Not delayed	24	28	13	65
Less than 6 months	19	9	4	32
Between 6 and 12 months	18	21	9	48
Between 12 and 18 months	15	15	4	34
Between 18 and 24 months	4	6	—	10
24 months and above	7	6	—	13

Source: H. T. Parekh, "Follow-up procedures and practices" (paper prepared for the Interregional Symposium on Industrial Project Evaluation, Prague, 11-29 October 1965 (CID/IPE/C.1)).

[a] The data refer to a group of projects partly financed over recent years by the Industrial Credit and Investment Corporation of India, Ltd.

tivities and of deliveries of materials has lengthened the time for completion; or, because of insufficient foresight, technical plans have been subjected to various changes after the project has been started.

Broadly, the sources of these delays may be found in either inadequate forward planning of individual projects or organizational deficiencies in governmental administration, though these two causes are often inextricably interrelated.

The inadequate forward planning of individual projects often simply reflects the fact that the government departments responsible for the preparation and execution of projects do not have sufficient technical staff, such as surveyors, architects and engineers, to cope effectively with an expanding investment programme. Equally important is the lack of cadres with the competence and training to plan and manage the preparation and execution of projects efficiently. Both in the pre-construction and construction phases there is need for considerable managerial skill in co-ordinating and synchronizing the numerous separate activities which require to be undertaken by different government departments and private contractors; in this respect, the training of staff in modern management techniques can be of substantial assistance.[8] But the better forward planning of projects is not only a question of the adequacy of trained staff; it is also a matter of the standards set by the central agencies responsible for the approval of projects. Rigorous insistence by the planning agency and ministry of finance on the preparation of thorough reports before projects are approved can contribute significantly to the lessening of delays. In view of the difficulties occasioned by inadequate project preparation, it is not surprising that in the developing countries with some years of planning experience there has recently been a return to the practice of requiring projects to be prepared in detail before they are accepted for inclusion in the annual plan and budget. In India, for example, it has recently been stipulated that "no new scheme will be included in the annual plan unless it is fully worked out in all details and unless there is reasonable assurance that requisite resources are available for its completion as scheduled".[9]

Even when there has been adequate technical preparation of projects and both the financial and the real resources have been available for their execution, delays in initiation and construction have often arisen because of cumbersome and inefficient administrative procedures in government. Frequently, responsibility for different aspects of the financial, legal and technical work involved in project construction is shared by several government departments, and there is a lack of clear allocation of responsibility for overseeing and co-ordinating the work of project execution. Delays arise, for example, because land sites have not been purchased, because licences for materials have not been issued or because ancillary services of government departments have not been provided as promised. Moreover, there has often been a failure to distinguish clearly between decisions which can be taken by the civil service administrator and those which should be left to technical experts: authority for decisions of a technical nature has sometimes been concentrated in the hands of administrators who lack the necessary technical knowledge or experience. To establish a clear line of responsibility, some countries have resorted to the practice of establishing "project boards" for each project, or, in the case of major projects, they have formed separate public corporations to manage the construction of the project.

A particular, but very widespread, source of such administrative delay has been the excessive centralization of responsibility in the ministry of finance for the sanctioning of items of expenditure. The meticulous scrutiny of all items of expenditure by a central authority prior to their authorization, while conducted in the name of economy and public accountability, has frequently been an important cause of inefficiency and waste in project execution. This has been the recent subject of administrative reforms in a number of countries. In Pakistan, for example, the various ministries have recently been empowered, with some minor limitations, to sanction expenditures from budget grants without reference to the Ministry of Finance; at the same time, a system of financial, advisory units has been built into the ministries in order to promote efficient management of financial affairs.

In connexion with such reforms, however, it is pertinent to note a past comment of the Indian Estimates Committee that "even where there are delegations of power and the administrative Ministry could normally take decisions itself, it has often resorted to consultations with the Ministry of Finance in order to escape any criticism later on".[10] The root of the problem, in other words, does not simply lie in the procedures followed by the ministry of finance. It is to be found in the larger difficulty that

[8] For instance, in a paper submitted to a recent meeting, Tarlok Singh stated that "the use of network planning techniques is to be strongly recommended for better management of the construction stage". See "the preparation and implementation of major development projects", presented to the International Group for Studies in National Planning, Caracas, 15-22 November 1966.

[9] Government of India, Planning Commission, *Fourth Five-Year Plan—A Draft Outline*, p. xiii.

[10] Government of India, Report of Estimates Committee, "Administrative, financial and other reforms", quoted in A. H. Hanson, *The Process of Planning: A Study of India's Five-Year Plans 1950-1964* (London, Oxford University Press, 1966), p. 275.

civil servants in the middle and lower levels often suffer from an unwillingness or incapacity to take decisions. And this is not unique to the ministry of finance but is common to many branches of government. In the context of Latin America, for instance, it has been observed that

> "there is relatively little room for delegation of authority both because of the low level of competence of intermediate echelons of the public service and of the reluctance of the middle layers to take on or accept responsibility for policy decisions".[11]

In many of these countries, the problem of inordinate bureaucratic delay and indecision has been circumvented by the creation of large numbers of autonomous agencies with discretionary powers over their financial and other affairs. But this has been criticized as a "solution which in fact does not solve the problem at all".[11] This solution has been described as

> "the excessive fragmentation of the administrative machinery by the creation of autonomous agencies which do manage to decentralize somewhat the decision-making process but at the cost of ruining the mechanism of centralized control, evaluation of performance, and establishment of working norms. Thus, some flexibility in decision-making is attained only by impairing the mechanism for administrative co-ordination".[11]

Clearly, whether the balance in administrative organization should be shifted towards greater centralization or greater decentralization is something which can be decided only in the conditions of each country. It is evident, however, that the problem is not solely a matter of changes in administrative practices; it is often, as much, a question of improving the quality of national civil services, particularly in the middle and lower echelons.

In general, it may be said that the improvement of efficiency in project execution usually calls for the enforcement of more rigorous standards in the forward planning of projects and for administrative changes both to establish clear lines of responsibility for execution and to simplify procedures. A major condition for such improvement is the strengthening of the staff in the various ministries capable of undertaking the forward planning and management of project execution.

CONTROL AND RATIONALIZATION OF CURRENT EXPENDITURE

Whereas much attention has usually been given in medium-term plans to the programming of public development expenditure, and particularly investment expenditure, current expenditure has generally been much more cursorily treated. So far as medium-term plans have discussed current expenditure, their main intent has been to emphasize the need to curtail the growth in such expenditure. In other words, the focus has been upon the limitation of current expenditure as a way of enlarging the resources available for investment; it has been considered as an adjunct to the intensification of efforts to raise revenue. This prescription has been in keeping with the dominant role accorded to capital accumulation in economic development. In practice, however, current expenditure in most developing countries has persistently increased more or less in line with revenue, and the desired increase in the surplus on current account has not materialized.

More recently, it has come to be recognized that prescription in terms of a choice between current and capital expenditure presents an oversimplified and misleading statement of the problem. It both ignores the contribution of certain recurrent expenditures to the improvement of co-operant factors of production[12] and fails to recognize the complementary nature of many items of capital and current expenditure. Certain outlays, such as those on education, health, research and agricultural extension, which have been traditionally regarded as recurrent, have come to be recognized as essential to the development process; and it is also evident that many public investment projects demand future increases in recurrent expenditure for their operation and maintenance. Thus, the prescription in favour of a general curtailment of current expenditure is not only unrealistic but may prove detrimental to the development effort. There is, none the less, an obvious need for selective control of current expenditure to eliminate waste of scarce resources. But, while the introduction of development planning has stimulated the more systematic scrutiny of investment expenditure, current expenditure has generally not been subjected to a similar evaluation. What, ideally, may be called for is a long-term framework for scrutinizing public expenditure in its totality.

Some of the factors accounting for the upward trend in current expenditure are common to all countries. They reflect not only the prevailing concept of the role of government but also the complementarity between demand for public services and the growth of national output. Economic growth,

[11] Roberto Campos, "Public administration in Latin America", *Public Administration—A Key to Development* (Burton A. Baker, ed.), 1963, p. 45.

[12] Recognition of the importance of certain outlays for development has engendered a movement away from the traditional distinction between recurrent and capital items towards the concept of development expenditure. The aim, generally, has been to group together all expenditures, whether current or capital, that contribute to economic development as opposed to those which are designed to maintain or increase current welfare.

moreover, has generally been associated with the increasing complexity of public organizations and functions. A further powerful force behind the increase in public expenditure has been the growth in political power of the lower-income groups of society and the spread in demand for welfare services.

The upward trend in public current expenditures is reinforced in developing countries by the crucial role which the public sector is called upon to play in the development effort. Much of the growth in current expenditure in developing countries has, in fact, been related in one way or another to development. The expansion in general administration, while sometimes excessive, has been associated with the larger role of government in economic life; and since civil service salaries in developing countries tend to be higher relative to *per capita* income than in developed countries, this has accelerated the upward movement in current expenditure. The substantial investment in infrastructure—transport, communication, power and water supplies—has enlarged the costs of operation and maintenance, some of which are charged to current account. Further, outlays on health and education, which serve the double purpose of contributing to current welfare and improving the productivity of the population, have generally risen strongly. Finally, it should be noted that subsidies and transfers have been used by many countries to further their economic policies; price supports for agricultural products or the subsidization of fertilizers have been common instances.

Of course, current expenditure in many developing countries has also expanded strongly in response to social objectives. The "welfare state" concept has been embraced by many of these countries. Closer communications between village and city and between developing and developed countries, together with the greater political power of low-income groups, have engendered rising expectations and stronger demands for social services. And the assumption of a welfare role has been more burdensome for developing countries where population growth is higher and the misery to be relieved is greater.

In both economic and social services, however, there has generally been much evidence of irrationality in the use of resources when patterns of expenditure are compared with avowed social and economic objectives. The scale of priorities among objectives has not been actively translated into expenditure programmes. For example, the uneconomic pricing of public services and the subsidization of public enterprises has persisted despite emphasis on the need to increase public saving; and even when changes in fiscal systems designed to raise more revenue have been introduced, the rate structures of public services have sometimes been allowed to remain unaltered. Or social welfare programmes have been expanded while plans have called for restraints on growth of consumption to raise investment and future output. Or educational programmes have not taken into account the future manpower requirements of the economy, sometimes giving rise to the paradoxical situation of unemployment among educated people in skill-deficient countries.

Instances of inconsistency between current expenditure programmes and avowed objectives are many and familiar, and they need not be exhaustively enumerated here. But it is worth stressing that the lack of co-ordination in public programmes also extends to the relation between capital and current expenditure. Many forms of public investment generate future increases in recurrent expenditure, and when this is taken into account in plan formulation, it may reveal the need for changes in the investment programme in order to ensure that other aims, such as a larger current account surplus, are met. In the 1962-1968 Nigerian development plan, for instance, the treatment of recurrent expenditures as a crucial variable led to the choice of a lower level of investment and the shifting of investment to productive sectors.[13] The strategy was based on the observation that

> "investment in administrative sectors not only is less directly productive in economic terms, but reduces budget surpluses by a factor of three compared to economic sector projects in generating recurrent expenditure . . .".[14]

To promote their rational scrutiny, items of current expenditure have to be viewed within the framework of general economic and social objectives and of total public expenditure. This can help to ensure that resource allocation is made in accordance with the priorities established for public spending as a whole. While the evaluation of items of current expenditure against national objectives and prospective resources is no new problem, a number of countries have made attempts in recent years to strengthen this process by considering the growth of expenditure within a longer-term perspective.

Some countries have sought to establish guidelines for the growth of current expenditure within the framework of their medium-term plans. In preparation of their plans, most developing countries have, of course, set targets for the growth of total current expenditure. But generally, these targets have been

[13] Federal Republic of Nigeria, *Progress Report, National Development Plan, 1962-1968* (Apapa), p. 46.

[14] L. M. Hansen, "Comprehensive economic planning in Nigeria" (United Nations Economic Commission for Africa document E/CN.14/CP/7), p. 5. It was estimated that while ten units of capital outlay in the economic sector engendered a unit of recurrent cost in each subsequent year, in the social and administrative investments a unit of recurrent cost resulted from five and three units of capital, respectively.

no more than the balancing item between the financial resources expected to become available and the planned public investment programme; they have not reflected independent estimates of the expected or planned growth in current expenditure. In some of the countries with considerable planning experience, however, quantitative guidelines have been established for major components of current expenditure though even in these countries, as can be seen from table 2, the coverage of items has usually been quite incomplete.

In certain instances, such guidelines appear to have been based on quite careful scrutiny and evaluation of future requirements. In France, assumptions about

Table 2. Selected countries: Quantitative guidelines for total current expenditure and components as outlined in medium-term plans

Country	*Total*	*General administration*	*Economic services*	*Education*	*Health*	*Research*	*Debt service*	*Subsidies and transfers*	*Other*
France		X						X	X
India	X								X
Pakistan	X	X					X		X
Turkey				———X———			X		X
United Arab Republic	X	X		X	X	X	X	X	X
Venezuela	X	X	X	X	X		X		X

Source: National development plans.

Note: For France, Pakistan and the United Arab Republic, data refer to reference year and terminal year; for Turkey and Venezuela, annual figures and annual rates of growth; for India, Pakistan and Venezuela, total plan figures. For India and Pakistan, data refer to non-plan outlay and non-development outlay, respectively.

certain aspects of government policy have been explicitly made in assessing prospective trends in particular components. Where a long-term programme has been drawn up—as, for example, the educational programme in Turkey—this has also provided a basis for defining guidelines. In the main, however, the forward planning of targets for components of current expenditure has not been of a comparable nature to that undertaken in the preparation of investment or development programmes. In India, Pakistan and the United Arab Republic, for instance, the targets appear to have been based mainly on projections of past trends.[15] Still, even such exercises may have helped, in some measure, to induce a more rational approach to current expenditure and to instil a greater spirit of discipline in the control of outlays.

Multi-annual budgeting, not necessarily associated with medium-term planning, has also been experimented with by certain developed, as well as developing, countries in recent years. Multi-annual planning, for example, has been used for some time in the United Kingdom Ministries of Education and Transport as well as in the United States Department of Defense. A more comprehensive attempt has also been made in the United Kingdom to draw up a perspective for public expenditure as a whole. A report,[16] prepared in accordance with the recommendations of the Plowden Committee,[17] projected actual public expenditures in 1963/64 to 1967/68 "on a basis of the government's present policies and programmes". Some of the difficult points encountered in this exercise were the choice of assumptions about the future levels of agricultural support and debt servicing. It was decided that since expenditure for agricultural support is affected by changes in supplies and market prices the best procedure was to assume that the prevailing level would be maintained. Debt servicing was excluded since "the forecasting of it is dependent on a number of arbitrary assumptions about the level of expenditure, taxation and interest rates over the whole of the intervening period". To compensate for possible underestimation of the cost of implementing the outlined public policies, a contingency fund of 2 per cent of total projected expenditure was added.

It is true of all these exercises that, since public expenditure is subject to annual legislative vote,

---

[15] But in India and Pakistan, those items of current expenditure which have been classified as plan or development expenditure have been subject to the same scrutiny as planned investment expenditure.

[16] United Kingdom, Chancellor of the Exchequer, *Public Expenditure in 1963-1964 and 1967-1968* (London, 1963).

[17] The Committee was set up to make recommendations for controlling public expenditure. In its report, *The Control of Public Expenditure: Plowden Committee Report* (Cmd. 1432), the Committee envisaged a five-year programme for current and capital accounts in which the first year programmes were to be considered firm; second year, firm but subject to major changes; third year, provisional; and fourth and fifth years, tentative.

Governments may not be able to adhere to their targets if these do not meet with the concurrence of the legislatures. But the same also holds for investment or development expenditure. Among countries engaged in medium-term planning, perhaps a greater weakness is the fact that, while planning agencies have generally been the bodies primarily concerned with the establishment of targets, they have usually played little or no part in preparation of the annual budget for current expenditure. Whereas planning agencies have commonly participated in the drawing up of the annual investment or development budget, ministries of finance have continued to regard preparation of the current account budget as their prerogative.

In general, it may be said that. while flexibility in public expenditure programmes has to be retained, most Governments could do more to exercise a selective control over the growth of current expenditure. More consideration could be given to the enunciation of quantitative guidelines within the context of medium-term plans or forward-looking budgetary appraisals. By reflecting considered priorities, these could help to strengthen control over current expenditure and to improve the allocation of resources within the public sector.

MOBILIZATION OF DOMESTIC RESOURCES FOR PUBLIC SECTOR PROGRAMMES

The available evidence indicates that total government expenditure has increased sharply in most developing countries; usually, its rate of increase has been appreciably higher than that of national income or output. But generally, this has not been accompanied by a corresponding increase in the level of current revenue; and the gap between total expenditure and current revenue has been financed by reliance on external resources or domestic borrowing.

This is not the place to discuss the role of external resources in supplementing domestic resources or in relieving foreign exchange scarcity. It is sufficient to note that the availability of these resources does not lessen the need to raise more revenue in developing countries. On the contrary, even apart from other considerations about the importance of self-help policies, the mounting problem of servicing current and prospective external debt itself demands that steps be taken to increase current revenue. In addition to the shifts in the balance of payments required to meet the external transfer problem, the rising external indebtedness also accentuates the internal problem of making more resources available to the public sector.

In addition to dependence on external resources, Governments have commonly sought to transfer resources to the public sector through domestic borrowing or inflationary financing. Some of the measures pursued have been of a long-term nature designed to raise saving propensities in the private sector. For instance, contractual savings, such as those embodied in the social security schemes of a number of Latin American countries and the United Arab Republic or in the provident fund arrangements of some Asian countries, have proved to be a not insignificant means of raising the level of private saving and of transferring resources to the public sector. Likewise, some developing countries have sought to strengthen the propensity to save through the promotion of government bonds as well as through the creation of post office savings banks, rural thrift societies and agrarian banks. In the main, however, the transfer of resources to the public sector by methods other than taxation has been accomplished by inflationary means, since significant changes in household saving necessarily take place only over the long run and primarily in response to the growth of income. In most developing countries, there has been a certain amount of room for expansion of the money supply without running the risk of intensifying pressure on the price level either because of the existence of underutilized resources or, more commonly, because of the gradual monetization of the economy. But, in practice, the use of inflationary financing to bridge the gap between expenditure and revenue has frequently gone far beyond this point and has become a chronic problem in some countries.[18]

Thus, whichever way the problem is looked at, the expansion in the current revenue of Governments emerges as an inescapable element of development policy. It is a familiar characteristic of a large majority of developing countries that current revenue of general government amounts to no more than 15 per cent of gross domestic product. There are in fact many countries—such as Colombia, Guatemala, and Honduras, to name only a few from Latin America—where the figure is about 10 or 11 per cent. In developed countries, by contrast, current revenue of general government is usually of the order of 25 to 35 per cent of their gross domestic product. Given the many responsibilities which Governments have assumed and the many others which they expect to assume, both in the provision of current amenities for their peoples and in speeding up economic development, it would appear that within the span of a development perspective of fifteen to twenty-five years the level of current revenue in relation to gross domestic product in those countries where it is at present low might

[18] A fuller discussion of this problem is contained in: Roque Carranza, "Development and stabilization policies in Latin America: Some problems" (E/AC.54/L.4).

have to be nearly doubled. A perspective of this sort is important to bear in mind, for it helps in formulating and enforcing the required measures year after year. It is true that a small number of developing countries already manage to collect one fifth or more of their gross domestic product as government revenue. But even in such cases appropriate reforms can lead to substantial improvements in revenue and, through reform in the revenue structure, in the functioning of the production system.

Taxation being the largest component of current revenue, a heavy onus for mobilizing resources rests on tax policies. Unfortunately, however, the plans of developing countries have not, in general, been notable for providing operational content to their design for taxation. Plans have not spelled out the implications of the desired development programmes in terms of the needed increases in taxation. But the experience of the few developing countries which have made systematic efforts for designing a tax programme as part of their over-all development plans indicates that the guidance of fiscal policies can be facilitated if the taxation targets are stated in some detail. In India and Pakistan, for example, each successive development plan has provided indications of, first, the tax revenue expected from projected income and output at prevailing rates of taxation, and, secondly, the additional taxation intended to be raised through new policy measures. An attempt has been made to provide some indication of the contribution to be made by both federal and state governments as well as by principal sources of revenue. The plans cannot obviously establish tax targets in great detail; it is in the nature of things that the precise contours of each tax measure have to be worked out by the finance ministry as part of the annual budget in the light of prevailing circumstances. But in establishing some broad targets for resources to be mobilized through taxation—an exercise which has to be carried out in collaboration with the finance ministry—the plans have helped to guide the policy makers in working out the necessary measures in accordance with plan priorities.

In over-all operational terms, what these two countries have done is to provide a framework for raising the level of tax revenue every year as part of the plan-implementation process. The recent experience of India and Pakistan, incidentally, suggests the magnitude of the results that can be achieved when concerted efforts are made. In Pakistan, the second development plan lifted the ratio of tax revenue to gross national product from 6.1 per cent in 1959/1960 to 8.7 per cent in 1964/1965, or by about 2½ points over a five-year period.[19] In India, the country's third five-year plan which covered approximately the first half of the 1960's succeeded in raising the ratio of tax revenue to national income from 9.6 to over 14 per cent.[20] However, the comparatively large increase in this case—about 4½ points during five years—was compounded of two unusual developments: the large increase in taxation under the influence of hostilities with mainland China and the slow expansion in national income owing to abnormally poor harvests. During the preceding plan period, which approximately covered the second half of the 1950's the increase in the tax ratio amounted to about 2 percentage points. Such examples suggest that, if vigorous measures are enforced, many developing countries may frequently be able to raise the ratio of tax revenue to national output or income, expressed as a percentage, by about half a point *per annum*.

The particular tax measures which can be most suitably employed are bound to vary with the conditions prevailing in each country. But there would probably be general agreement about the main characteristics which a desirable tax structure in most developing countries should possess. One is that it should restrain the growth of consumption in favour of higher levels of saving and investment. Another is that it should influence the allocation of resources within the private sector in the directions suggested by plan priorities. At the same time, it should also encourage more efficient utilization of scarce resources, such as capital, land and foreign exchange. In conformity with social objectives, moreover, the tax structure should bring about a more equitable distribution of income and wealth. Finally, there are some specific characteristics of the tax structure which are rather technical conditions for ensuring that the tax structure better serves its more general aims; these include a broad tax base, a relatively high revenue elasticity, ease in administration and efficiency in collection. It is towards the strengthening of such features that the gradual reform of the tax structure should be directed. In the following paragraphs, the kinds of changes which are required are discussed briefly with reference to particular measures.

In order to enlarge the supply of resources for productive investment, tax measures can help to restrain the expansion in private consumption. A personal income-tax, for instance, is commonly employed as a means of raising resources by controlling the level of disposable income and thereby the level of private consumption. Although the number of developing countries which make use of a personal income-tax has steadily increased over the years,

[19] Government of Pakistan, Planning Commission, *The Third Five-Year Plan (1965-70)* (Karachi, 1965), p. 70.

[20] Government of India, Planning Commission, *Fourth Five-Year Plan—A Draft Outline*, p. 15.

its contribution to total revenue has remained comparatively small. In many developing countries, there is need for broadening the definition of personal income so as to include not only salaries and wages but also such items as rents, interest, dividends and royalties. In countries which employ a "schedular" system, involving taxation of income from different sources at different rates, a "global" approach might well yield a distinct improvement in revenue. The fact that in developing countries the minimum levels below which incomes are considered tax exempt are often very high—as high as fifteen or even twenty times the average level of *per capita* income—leaves a large proportion of the income-earners outside the tax fold. True, the less developed countries where a substantial part of total ouput arises in a multitude of scattered units cannot be expected to have, in this respect, a pattern similar to that prevailing in developed countries; however, the very high exemption limits that are currently maintained do not seem to be in consonance with the objectives of economic advance which the developing countries are eager to achieve. The yields from income-tax can be further improved by eliminating unnecessary deductions that are often allowed, ostensibly on grounds of social justice or for providing incentives, in computing tax liability. Tax revenue can gain still further through a systematic withholding of tax liability on current income, commonly called the "pay-as-you-earn" scheme. Experience has also shown that, in order to be fully effective, the personal income-tax has to be supported by a number of complementary measures, such as a tax on capital gains, in order to close avenues for evading direct income-tax.

Taxation of income is by no means the only way of influencing the level of consumption. Among developing countries, Ceylon and India have experimented with a tax on total consumer expenditure, in addition to a tax on personal income. Although in principle an expenditure tax has a great deal of merit, since it directly discourages consumption and promotes saving, these countries have found it administratively difficult to enforce, with the result that its yields have been rather small. Generally, in developing countries the major instrument of controlling consumption, and consequently the mainstay of government revenue, is the taxation of goods and services. Given their highly agrarian character, the wide dispersion of activity among small-scale producers and traders in both rural and urban areas, the comparatively small share of wages and salaries in total income, and the widespread illiteracy, developing countries find that taxes on goods and services provide the principal means of reaching large numbers of people. The plans of some of these countries, in fact, have explicitly recognized that the predominance of such taxes would continue for quite some time. While questions have been raised about the incidence of taxes on goods and services, policy makers have contended that these taxes are not necessarily more inequitable than income-taxes. An inquiry conducted in India some years ago, for instance, revealed that the country's taxes on goods and services were "mildly progressive", inasmuch as their incidence increased with expenditure level in both rural and urban areas.[21] Furthermore, as the policy makers have maintained, the question of equity has to be judged not only on the basis of the taxes paid by individuals but also against the yardstick of the outlays of Governments on such items as education and health incurred primarily for the benefit of the poorer people.

Following this mode of thinking, several developing countries have found in excise duties an important tool of resource mobilization. By imposing excise duties on a wide range of goods, Governments have been able to reach large numbers of people who are normally not subject to income-tax and to obtain from them, in the words of the Pakistan plan, "some contribution to national development".[22] These duties have provided substantial revenue to Governments. At the same time, through the application of differential rates, they have served to influence the composition of output in the private sector. Heavy taxation of luxury or semi-luxury commodities has helped to limit demand and investment in these lines of production. In some instances, moreover, the restraining influence of these duties on private consumption has been employed to create exportable surpluses of selected products of domestic industries and thereby to enlarge the supply of one of the scarcest resources for development, namely, foreign exchange.

In some countries, a parallel, and often supplementary, role to excise duties is played by sales taxes. In developing countries, the task of revenue collection is facilitated if the levy takes the form of a general sales tax imposed at a specific point in the chain of transactions rather than of a turnover tax. By establishing different rates for different groups of commodities, considerations of equity, as well as of resource allocation, can be introduced into the system. Whether the sales tax should be at the wholesale or retail stage would naturally depend upon the circumstances of a country. There is little doubt, however, that sales taxes and excise duties are particularly suitable instruments of resource mobiliza-

[21] Government of India, Ministry of Finance, *Report of the Taxation Enquiry Commission, 1953-54* (New Delhi, 1955), vol. I, pp. 68-69.

[22] Government of Pakistan, Planning Commission, *The Second Five-Year Plan (1960-65)* (Karachi, 1960), p. 52.

tion, and Governments in many developing countries need to make more effective use of them.

It is not only because development requirements are increasing that the need for excise and sales taxes has arisen. These taxes are also favoured because it is generally believed that the scope for taxes on exports and imports is diminishing. In export-oriented countries, taxation of exports—through imposition of duties or through multiple exchange rates—has often in the past, by virtue of the ease of collection, provided a major means of revenue for Governments. But recently, except in a few developing countries whose exports have continued to be in buoyant demand, the relative importance of export taxation has been dwindling. In many countries where export promotion is a major aim, the elimination or drastic curtailment of export taxation has become an avowed part of official policy. It is now recognized that export taxation serves a purpose only on infrequent occasions when windfall profits resulting from currency devaluations or external booms have to be siphoned off.

Likewise, planners in developing countries have commonly expected that the relative importance of import duties or of profits obtained through multiple import rates would also decline. It is reasoned that developing countries would continue to promote import-substitution in a vast variety of goods, and that consequently the scope for import taxation would diminish. So far as imports of capital equipment, key intermediate goods and essential raw materials are concerned, it is pointed out that such items are generally admitted without duty. These arguments have a great deal of validity. However, it has also to be borne in mind that the process of economic development does not necessarily imply that the level of imports in relation to gross domestic product will diminish. This consideration alone suggests that the scope for import taxation need not necessarily be small. Furthermore, while imports of capital equipment and other strategic goods have to be accorded priority, these imports need not be exempt from taxation. As noted earlier, an important function of fiscal policy is to achieve more efficient utilization of scarce resources, and often in developing countries few other resources are as scarce as is foreign exchange. Yet, for a variety of reasons, the import cost of machinery and other key items has usually been allowed to remain much lower than their true scarcity value. Thus, where the cost of such goods is not an obstacle to development and where complementary inputs are forthcoming, some element of taxation on imports of capital goods and other priority items may be quite desirable. In Pakistan, for example, where this problem has received some attention, the planners have felt that even government imports should be subject to taxation "so that the public sector has a measure of the true scarcity value of the foreign exchange allocated to it".[23]

In the sphere of agriculture, too, fiscal policy can be of material help in bringing about a more efficient utilization of resources. Because of the highly scattered nature of rural activity in developing countries, it has generally been quite difficult to extend income-tax to agriculture, and some form of land tax has traditionally been the mainstay of agricultural taxation. But over the years, particularly in Asian and Latin American countries, because of substantial increases in prices and, to some extent, of some non-economic factors, the contribution to the revenue from land taxes has diminished substantially. It has been argued that the pivotal element of reform should consist in taxing agricultural land on the basis of its economic potential rather than its present yield. And this can be done without carrying out extensive cadastral surveys which require considerable time and resources. If agricultural land is classified into a few broad categories after allowing for differences in soil, climate and other relevant factors, and these categories are subjected to graduated rates of taxation according to their economic potential calculated on the assumption that land was efficiently cultivated, this can not only yield additional revenue but can also, by penalizing inefficient cultivators, promote better land use and management. Such a tax may be suitably coupled with surcharges on absentee owners of agricultural land, penalty charges on cultivable land left idle and favourable treatment of newly reclaimed land or the land that is shifted to new uses according to plan priorities.[24]

In calling for reform of agricultural taxation, policy makers have not been oblivious of the need for adequate incentives for farmers; but they believe that the really effective incentives are those which work through subsidized and assured supply of such important inputs as fertilizers, improved seeds, advisory technical services, credit at low interest rates and upward revisions in agricultural prices rather than through extensive tax remissions. In fact, there is frequently a need for diverting a part of the gains made by cultivators through irrigation and other rural development programmes sponsored by the Government. The planners in India and Pakistan, for example, have suggested upward revisions of irrigation-water supply rates and the imposition of "betterment levies" in such cases. The current official

[23] *Ibid.*, p. 50.

[24] H. P. Wald, "Reform of agricultural taxation to promote economic development in Latin America", in Organization of American States, Inter-American Development Bank and United Nations Economic Commission for Latin America, *Fiscal Policy for Economic Growth in Latin America* (Baltimore, 1965), pp. 326-336.

thinking in India is that irrigation rates should be fixed at 25 to 40 per cent of the additional net benefit to the farmer from the irrigated crop; and where it is not possible to measure net benefit the rate should be 5 to 12 per cent of the "gross income" from the irrigated crop.[25]

Similar reasoning has led to questioning of widespread use by Governments of total or partial tax "holidays" on business profits for specified periods of time. Some taxation of business profits is not necessarily a significant deterrent to private capital formation. It has been a common experience that a sustained increase in aggregate demand, a generally stable environment and an orderly supply of essential inputs, including foreign exchange and selective financial assistance, are far more conducive to private initiative than are extensive tax concessions. Some system of tax incentives has nevertheless been desirable as a means of influencing the allocation of private investment in directions which conform with plan priorities. But this gain has had to be balanced against the potential loss of revenue in selecting the form of tax concession; and on this score there is some presumption in favour of accelerated depreciation or initial allowances as compared with outright tax holidays. While the former do not entail any permanent loss of revenue, they help to reduce the riskiness of new investments and to improve the liquidity of investors in the early years of a new enterprise.[26] The stronger incentive offered by tax holidays may, in some circumstances, be deemed to be necessary but, in view of the importance of raising revenue, their sparing use is advisable.[27]

Policies designed to mobilize resources and to influence their allocation and utilization can also encompass the additional aim of improving the distribution of income and wealth, to which Governments in developing countries have attached considerable importance. Often Governments have come to power on the basis of a specific mandate on this score from their people. There is also the underlying belief that unless the vast majority of the people are convinced that they are making relative gains they will not lend whole-hearted support to development policies. Taxes of various kinds help to achieve such an objective. For example, it is universally recognized that the system of personal income-tax needs to contain a strong element of progression, though at the same time progression should not be carried so far as to become a hindrance to private initiative. Mark-ups on trading transactions are commonly high in developing countries, and the taxation of trading profits offers another means for improving the distribution of income. A tax on property can similarly serve an important purpose, as the experience of several countries shows. Particularly in countries where the very large size of agricultural holdings is considered undesirable on grounds of both equity and efficiency, a suitably designed tax on rural property may help to achieve more viable agricultural units. Further, with the rapid urbanization taking place in many countries, urban land values have generally been increasing sharply, and there has been considerable scope for taxation of speculative gains. Finally, such measures as a tax on net wealth, an estate or death duty and a tax on gifts made during the lifetime of the benefactor are also of long-run importance in improving the distribution of income and wealth.

Whatever tax system a country may establish to suit its own particular circumstances, it needs in any event to foster resiliency in the tax structure so that as national income or output increases the intake of tax revenue registers a proportionally larger gain. A progressive rate structure of taxes on income and on other suitable variables serves as an essential plank of such an endeavour. Similarly, taxes on goods and services need to be imposed on an *ad valorem* rather than specific basis, since the former respond automatically to price increases and thereby improve the elasticity of tax yields. Further, an effective tax system also requires parallel steps to modernize and streamline the machinery for tax administration. As the plans of some developing countries have themselves recognized, measures are urgently needed to simplify and rationalize the tax system, to remove loop-holes in tax laws, to prevent tax evasion, and to reduce delays in actual receipt of tax revenue by Governments through shortening the time lag between levy and collection and through more efficient tax administration.

In sum, the effectiveness with which plans are implemented depends in no small measure on the readiness of Governments progressively to reform tax structures. Fiscal measures are a powerful instrument of implementation and their vigorous and skilful use can spell the difference between success and failure in implementation.

---

[25] Government of India, Planning Commission, *Fourth Five-Year Plan—A Draft Outline*, pp. 87-88.

[26] A further argument advanced in favour of tax holidays has been that, unlike accelerated depreciation or initial allowances, they do not discriminate in favour of capital-intensive activities. In view of the low elasticity of substitution between capital and labour in most manufacturing processes, however, this consideration is generally not of practical importance. Moreover, such allowances can be granted selectively so as not to encourage investment in activities, such as materials handling, where there may be a relatively high elasticity of substitution.

[27] Many countries have also utilized tax holidays in order to attract foreign private investment. The inducements offered by individual countries have probably been cancelled out in part by the fact that other countries have been extending similar concessions.

SUMMARY

Annual planning and the fiscal budget

A continuing problem which faces all countries in the execution of medium-term plans is the management of budgetary and other short-term policies for minimizing the adverse effects of changing circumstances on the progress of plan implementation. The flexible conduct of policies within the framework of a medium-term plan is a major condition of success in implementing development plans. The preparation of an annual plan or a national economic budget for one year merits far greater attention than it has received in the past in developing countries. There is, moreover, a strong need for an active role by the planning agency in such work.

In developing countries, in order to assess whether a tolerable over-all equilibrium will be maintained, it is necessary to estimate not only the likely demand-supply balance at the aggregative level but also the likely balance in markets for critical commodities and productive resources. The well-known short-run instability in domestic agricultural production and export earnings which faces most developing countries accentuates the importance of estimating these specific demand-supply balances.

Construction of foreign exchange budgets and the evaluation of financial balances within the public sector, which several developing countries have attempted, are valuable aids in policy-making. These are not, however, substitutes for over-all annual or short-term planning. While no general prescription can be made about the kinds and number of specific balances which are relevant for assessing the consistency of short-term policies in developing countries—these are bound to vary with the individual circumstances of each country—the frequency with which bottle-necks arise in most countries suggests that greater attention to specific balances as tools for the exercise of policy measures can improve short-term management of the economy.

Programming and execution of annual development expenditure

In order to bring greater order and coherence in their public expenditure programmes, developing countries need to devise arrangements for ensuring that projects and schemes included in the annual budget are consistent with the public expenditure programme outlined in the medium-term plan.

Traditionally the function of financial appraisal and control has been discharged by the ministry of finance. However, the introduction of development planning has almost always required administrative changes to reconcile budgetary programming of development projects with these more traditional functions. The specific organizational changes which are made to integrate planning and budgeting are bound to vary from country to country. But the experience of these countries in which planning has been practised for some years suggests that these changes should be directed not towards the circumvention of the ministry of finance or the reallocation of some of its functions to a separate and independent agency but towards the fusion of its work with the functions of the planning agency and the executive ministries through the creation of common machinery.

Co-ordination of the work of the planning agency and the ministries in the preparation of the annual budget needs to be accompanied by steps to ensure that the proposed projects or tasks are carried out as planned. Delays in completing projects can be reduced through better forward planning and by removing deficiencies in administrative procedures. These, in turn, require larger numbers of trained staff, enforcement of rigorous standards for the approval of projects, and a clear allocation of responsibility among the departments concerned.

Control and rationalization of current expenditure

Governments in developing countries no doubt need to exercise restraint in the expansion of current expenditure. But this does not imply that all items of current expenditure must necessarily be curtailed. The speeding up of economic development in itself requires some growth in expenditure on such items as general administration, economic services, operation and maintenance of public projects, and education. Moreover, the rising demand for more social services must, to some extent, be met. In essence, what is needed is selective control of expenditure in order to eliminate waste of scarce resources.

To promote the rational scrutiny of items of current expenditure, these need to be viewed within the framework of general economic and social objectives and of total public expenditure. This would help to ensure that resource allocation is made in accordance with the priorities established for public spending as a whole.

Improvements can be made without sacrificing flexibility in current expenditure programmes by giving more consideration to the enunciation of quantitative guidelines within the context of medium-term plans or forward-looking budgetary appraisals. A clear reflection of the considered priorities of society in this manner can help to strengthen control over current expenditure and to improve the allocation of resources within the public sector.

Mobilization of domestic resources for public sector programmes

The expansion in current revenue of Governments is a crucial element of development policy. The effectiveness with which plans are implemented depends in no small measure on the readiness of Governments progressively to reform tax structures. Fiscal measures are a powerful instrument of plan implementation, and their vigorous and skilful use can spell the difference between success and failure in achieving plan objectives.

The task of raising revenue through appropriate fiscal policies is facilitated if the taxation targets are stated in some detail. Some broad indications provided in a medium-term plan help to guide the policy makers in working out the necessary measures as part of the fiscal budget.

There are certain general objectives which a desirable tax structure in developing countries should serve. Such a structure should be designed to restrain consumption in favour of higher levels of saving and investment, to influence the allocation of resources within the private sector in the directions suggested by plan priorities, to promote the more efficient utilization of scarce resources, and to favour a more equitable distribution of income and wealth. In order to achieve these objectives, suitable tax measures embracing taxation of incomes, goods and services, property and wealth need to be adopted and their scope steadily enlarged.

Chapter III

SOME PROBLEMS OF IMPLEMENTATION IN THE PRIVATE SECTOR OF THE ECONOMY

Introduction: Integrating the private sector into a plan

A development plan is the embodiment of official initiatives to bring about, in the course of a designated period, specific changes in the economy which would, in the planners' opinion, not otherwise occur.[1] However simple the content of the plan, its very purpose is to affect, either directly or indirectly, the economy as a whole. And since, in most developing countries, the bulk of the economy is in private hands—that is, most production and investment decisions are made outside the Government—the success of the plan depends not only on the ministries or official agencies that may be directly involved in its implementation but also on appropriate behaviour of individuals and business concerns.

Even when the plan has no explicit reference to the private sector, its rationale (and in some cases its actual execution) must rest at least on tacit assumptions regarding private decisions and actions of those who are to use the new facilities as well as those who must supply the necessary inputs. A plan whose content is confined to nothing more than a series of public investments in infrastructure can be justified only on the basis of decisions imputed to users of the new facilities, whether they be farmers expected to ship their produce over a planned road or manufacturers expected to absorb electric power from a planned generating station. And the execution of them has a similar implicit dependence on the private sector for the necessary inputs: though investment may be denominated in terms of financial outlays on roads and bridges, it has to be implemented in terms of cement and steel and other resources, frequently supplied by private producers.

Development plans have, in fact, tended to become more elaborate. Increasingly they are extending beyond the mapping out of a programme of public sector projects into the area of target setting for the economy as a whole. Targets may be set in the broadest terms (as in the case of over-all rates of growth in national income) or in physical detail (as in the case of the inputs and outputs of particular industries) or in terms of policy and quality objectives (such as rates of saving or price increase or literacy). Whether implicitly and in general, or explicitly and in detail, all such targets involve the private sector; and if the relevant elements in the private sector do not perform appropriately, the plan is unlikely to be fulfilled.

To recognize that the more comprehensive the plan, the more dependent it is on private sector performance is not to imply that the Government has to or can "implement" the plan in the private sector in the same way as it implements its own public sector intentions. On the contrary, recent experience indicates that many developing countries encounter major difficulties in implementing public sector plans and that their control over the private sector is at best very tenuous. Indeed, the problems discussed in this paper are, in general, the direct result of the absence of any assured means by which a Government can instigate in the private sector action that is necessary for the fulfilment of its plan.

There is no set of *a priori* principles which a Government can apply in order to induce the private sector to behave in a manner that is consistent with the needs of the development plan. Nor is there a large body of empirical evidence of the way in which relevant official action and methods have actually worked out: experience with planning among market economies is too short and the circumstances prevailing during plan periods too diverse to permit the distillation of definitive precepts. At best, the available record of the way in which planning has been undertaken can do no more than suggest some tentative conclusions with regard to the most com-

[1] The nature of these changes is not here at issue: it is assumed that they are desirable, feasible and mutually consistent and that the question is merely one of ensuring that they are effected. This is not to imply that all plans meet these criteria. Nor does it imply that the plan is rigidly frozen on formulation, to be implemented in every detail precisely as originally conceived. On the contrary, one major implementation problem is to provide for running adjustments to the plan as events unfold. And to bring the private sector into the adjustment process must be one of the specific purposes of the mechanisms used by the Government for associating individuals and business enterprises with the plan.

mon difficulties that have been encountered and hence some preliminary thoughts concerning ways and means of avoiding them.

In seeking to harness the key elements in the private sector to the purposes of the plan, the Government can adopt two distinct, but not mutually exclusive, tactics. It can act in such a manner that the private sector will come to identify its own interests with those of the plan, thereby prompting spontaneous action complementing that planned for the public sector. Or where, for whatever reason, spontaneous action is not forthcoming from the private sector, the Government can bring to bear a variety of policy instruments to encourage or impel the desired pattern of behaviour.

The main difficulties encountered in pursuing the second of these tactics stem from the fact that Governments possess a limited array of instruments with which to induce the private sector to conform and that these self-same instruments are the regular means of managing the economy on a day-to-day basis so as to maintain (or restore) stability. This problem of short-term management, moreover, tends to be a major preoccupation in most of the developing countries, partly because of their vulnerability to external influences (such as changes in export markets or in import availabilities or prices) and partly because of the strains set up by the effort to accelerate the growth process itself. Where a Government wishes to adopt a development plan the fulfilment of which is contingent on approximate action by private producers, there is thus a powerful reason for it to try to organize its planning procedures so that at least the key elements of the private sector are involved from the outset in a manner designed to harmonize their own interest with that of the economy as a whole. The closer the resulting sense of identity the less need there is likely to be to use official policy instruments to induce or deter particular actions by private concerns. Needed capacity will then be expanded not because of the offer of some tax advantage but because of the entrepreneur's confidence that the outlays to be made under the plan will increase the demand for the product in question to the extent necessary to justify the investment.

While such spontaneous conformity is a prime objective, it is never likely to be sufficiently comprehensive to allow Governments to dispense with more active ways of guiding the private sector. Not all private industries are likely to benefit from the plan. Indeed, the plan may require specific restraints on some elements and it may entail institutional changes that, while benefiting the economy in the long run, may be harmful to certain activities in the shorter run, and hence generate opposition.

Integrating the private sector into a development plan thus depends, at least in part, on the deployment of certain policy instruments to exert the necessary guiding influence on investment and production decisions. The problem facing the Government is to select the combination of instruments capable of inducing the required reaction in the private sector at the least possible cost to other objectives. For this purpose, it is necessary to appreciate the instruments and their limitations, so that they can be used circumspectly to encourage or discourage those elements in the private sector whose performance is crucial to the fulfilment of the plan.

Most control measures tend to be asymmetrical in their effectiveness: they are more successful in preventing investment than in promoting it. Rational reaction to incentives and other guiding policies is thus as dependent on the general economic environment as is spontaneous action in anticipation of demand changes. The more stable the economy and the greater the confidence of entrepreneurs in the Government's intention and capacity to minimize non-economic uncertainties the less is likely to be the difficulty in bringing the behaviour of the relevant elements of the private sector in line with the requirements of the plan.

THE RELATIONSHIP OF THE PRIVATE SECTOR TO A DEVELOPMENT PLAN

As a development plan extends, in concept and form, beyond a programme of investment financed by public borrowing or taxation, it depends increasingly on the appropriate performance of the production facilities (that are) in private hands. In an economy in which three fourths of the gross domestic product is generated in the private sector —and even higher ratios obtain in most of the developing countries—the mere designation of an average growth rate as a target for the economy as a whole implies a specific growth rate for the private sector, calculable after allowance has been made for the Government's declared intention with respect to the public sector.

Having started their planning experience with official investment programmes, most developing countries have now reached the stage of nominating over-all growth rates as central objectives of their plans, and an increasing number of countries have begun to spell out more detailed targets for particular industries, many of which are in private hands. Some plans have also embodied certain forms of structural change such as the relocation of particular industries, the development of particular regions or the reorganization of an existing system of land use. To a growing extent, therefore, the very process of planning has had to accommodate the private sector.

The progression is a natural one, for even a public investment programme must be premised on certain assumptions regarding the growth in taxable capacity and savings in the private sector and the ability of the Government to obtain the inputs for its own investment from domestic producers or in exchange for the exports of domestic producers. The more detailed the plan the less adequate are mere assumptions about growth in the private sector. And when the plan reaches the stage of a blueprint for accelerating growth and for effecting specified structural alterations in the economy, its chances for success depend very largely, in the first instance, on the extent to which the private sector actively co-operates. Experience shows that such co-operation cannot be taken for granted; it has to be assiduously cultivated.

This is particularly true in Latin America, where more of the economy is in private hands than in most countries in which planning has been attempted: all of agriculture, most of industry and in some cases even important elements of service and infrastructure such as transport, communications and power (see table 3). The record of co-operation between Governments and the private sector suggests that full mutual confidence has often been lacking. Private groups that have been dissatisfied with the performance of particular Governments in the field of economic administration have expressed doubts about their ability to carry through plans of a comprehensive nature. And contrariwise, the reluctance of some private interests to entertain changes in the *status quo* has often acted as a brake on development as conceived by government.

Some of these institutional features and social attitudes are likely to change only slowly. Economic development planning cannot wait on such changes. Indeed, the more rapid evolution of methods of planning and the achievement of some development successes, even in the public sector alone, may be expected to contribute significantly to the loosening of the rigidities which tend to hamper progress. In the circumstances, it would seem wise for Governments, while going ahead with public sector planning, to seek active private sector support both by building appropriate mechanisms for co-operation and by creating the climate in which individual enterprises can identify their own progress with that of the economy as a whole.

If the co-operation of the private sector is to be ensured, everything possible needs to be done by the Government to convince at least the relevant decision makers in the private sector that the fulfilment of the plan is in their own interests, that the designated public actions will in fact be carried through and that official policy will be geared to facilitating the implementation of the plan by the private sector. If this strategy is to succeed, it means that the key elements of the private sector need to be identified with the plan at an early stage, if not at the outset then at least before general objectives and priorities and detailed targets have been finalized. This, in turn, calls for methods of consultation not of a formal and perfunctory nature but substantive and continuous.

It is at this point that the initial difficulties of plan implementation in a market economy tend to arise. How can the strategic elements of the private sector be identified? Within these segments, who is to be consulted? How can the feasibility of the relevant private sector targets be tested? How can the credibility of government intentions be established so as to persuade individual entrepreneurs to act appropriately in anticipation? How can the co-operation of the workers best be assured? What provisions can be made for new industries? How can unorganized producers be properly motivated? How can performance be kept under effective surveillance so as to forestall emerging imbalances or to adjust plan targets?

To pose such questions is to bring home the fact that what has conveniently been referred to so far as "the private sector" is an abstraction with no simple counterpart in reality. To consult it and seek its involvement with a plan for development entails the making of practical arrangements for a continuing dialogue between the Government on the one hand and a range of producing entities on the other hand. This range may extend from relatively large corporations, in which the Government may itself share in ownership and control, all the way through to illiterate peasants disposing of minute quantities of produce in remote parts of the country. At the corporate end of the range, moreover, the entities with which the Government has to deal are likely to consist of separate components—management and labour—whose interests are in varying degree competitive and divergent. The mechanisms for associating "the private sector" with the plan have thus to be adapted to the degree of organization obtaining in all the relevant segments.

It is clear that there can be no general solution to this problem of effective consultation: institutional patterns differ so widely from one developing country to another that each is a unique case for which the most appropriate machinery and methods need to be separately sought, if necessary at the expense of a good deal of experimentation. However, even the limited experience so far gained in the area points to certain recurring questions to which something approaching a common answer may be inferred.

Table 3. Government participation in key industries in Latin American countries, 1965

Country	*Export industries*	*Domestic food production*	*Power*	*Transport and communications*			*Steel*	*Cement*	*Fuel*	*Machinery*	*Motor vehicles*	*Chemicals*
				Rail	*Water*	*Telephone*						
Argentina	—	—	D	D	D	—	D	A	D	A	A	A[a]
Brazil	—	—	D	D	D	D	B	—	D	A	A	B[a]
Chile	A[b]	A[c]	C	D	B	B	B	A	D	A	A	A[a]
Colombia	—	A[d]	D	D	—	D	D	A	C	A	A[e]	C[f]
Ecuador	—	A[d g]	D	D	—	B	—	A	—	—	—	B[f]
Mexico	—	A[c]	D	D	—	B	B	A	D	A	A	A[a f]
Peru	A[h]	A[i]	A	A	D	—	D	A	A	—	—	A[a f]
Uruguay	—	B[d g j]	D	D	D	D	—	D	D	—	—	B[a f]
Venezuela	—	—	C	D	D	D	D	—	A	—	—	B[a f]

Source: Centre for Development Planning, Projections and Policies of the United Nations Secretariat, based on United Nations Seminar on Organization and Administration of Public Enterprises, "Organization and administration of public enterprises, Report of preliminary study", July 1966;

Latin American Symposium on Industrial Development, organized jointly by the Economic Commission for Latin America and the United Nations Centre for Industrial Development in Santiago, Chile, 14 to 25 March 1966, "The process of industrial development in Latin America", vol. II (ST/ECLA/CONF.23/L.2/Add.1, 15 December 1965);

Report of the consultant group appointed jointly by the Economic Commission for Latin America and the Organization of American States, *Foreign Private Investments in the Latin American Free-Trade Area* (United Nations publication, Sales No.: 60.II.G.5);

Joint International Business Ventures, edited by Wolfgang Friedmann and George Kalmanoff (New York and London, 1965);

Transport Investment and Economic Development, edited by Gary Fromm (Brookings Institution, 1965);

United States Department of Commerce, *Overseas Business Review* (Washington, D.C.), various issues;

Business International, *Investing, Licensing and Trading Conditions in 50 Countries* (New York, 1966).

Note: The symbols indicate the approximate proportion of the output of the industry over which the Government exercises direct control by virtue of its ownership of capacity or its participation in equity: A=1% to 25%, B=25 to 49%, C=50% to 74%, D=75% and over.

[a] Petrochemicals.

[b] Nitrates.

[c] Sugar.

[d] Alcohol.

[e] Tires.

[f] Fertilizer.

[g] Milk pasteurization.

[h] Guano.

[i] Tobacco monopoly.

[j] Meat packing.

There would seem, for example, good reason to concentrate the Government's effort on those functions which are most important, conserving as far as possible its scarce administrative resources. In many cases, much of the private economy—most consumer goods industries and services and the bulk of the trading and financial sector—can safely be left to move voluntarily in the wake of plan-induced changes in demand. Leads and lags and minor imbalances in these portions of the economy are not likely to be too great to accommodate, nor are they likely to be cumulative to a degree that might threaten more important plan objectives.

The Government's organized relationship with the private sector can then be directed towards meeting two distinct and basic needs, one to ensure the widest possible knowledge and acceptance of the plan (leading to a general desire to assist in its fulfilment) and the other to ensure the active co-operation of the decision makers in strategic areas in which structural changes are envisaged or harmful bottlenecks might develop. The first of these functions may be served by a fairly large advisory body, as representative of the various elements of the private sector as possible, and capable of acting as an information channel through which the Government can discuss plan achievements and shortfalls as they become known. The second requires much more specialized machinery through which communication can be maintained with those industries whose performance is of crucial importance to the plan. In neither area has the record been notably successful.

It has proved difficult to convey to the population at large—and particularly to the agrarian and less literate elements—the purpose and modalities of a development plan. In few places have imaginations been captured and people motivated in a manner that would conduce to the achievement of output or productivity objectives. Where the effort has been made, the operational follow-through has not been forceful enough to overcome the inertia born of respect for tradition and fear of change; the symbols of the plan have not been translated into the reality that might stimulate action.

It has also proved difficult to establish a rapport with the decision makers in the industries that are deemed strategic. Governments often lack the qualified officials required to maintain a dialogue at the proper economic or technical level. In many countries, businessmen have a deep-seated lack of confidence in the Government. Often, moreover, they are suspicious of one another, so that in the case of an industry with an oligopolistic structure—very common in the relatively small markets of most developing countries—it is far from easy to organize operationally meaningful discussions of capacity, investment intentions and ways and means of meeting the demand postulated or implied in the plan. Within the industries in question, moreover, it is necessary to win the co-operation of the workers, organized in many cases in trade unions whose interests, while running parallel with those of the industries in which they operate, may diverge sharply from those of management.

Relations between government and private sector are thus likely to depend on many factors other than the formal institutional arrangements for consultation. As far as the latter are concerned, experience seems to point primarily to the need for flexibility: machinery that is suitable for one industry is not necessarily suitable for others whose organization and structure may be quite different. Facilities thus need to be provided for various types of consultation on a continuing basis, especially at the technical level but also at the more general policy-making level. Equally, no developing country is likely to be able to carry through a comprehensive plan without the means for maintaining a more or less continuous dialogue with key elements of the private sector: the producers of the major food and export items, the major capital goods and the major services.

The operation of such machinery will depend greatly on the Government's success in inspiring confidence in workers and investors and in persuading private business, the framework within which labour and management co-operate, to identify its interests with those of the economy at large. Recent history suggests that by demonstrating its capacity to carry through, in a prompt and efficient manner, its own announced development programme (i.e., of public sector investment) a Government is better placed to include the private sector in a plan: not only is confidence likely to have increased but the indirect as well as the direct impact of the official outlays and the resultant product will have illustrated the mutuality of interest between the public and private sectors. In the implementation of a plan, the public sector is on test no less than the private sector.

A country's ability to operate consultative machinery effectively may be expected to grow with experience and as familiarity with the planning process spreads. Two useful by-products may quickly materialize, however. For one, the Government may learn at first hand about the impact of its own policies, and it may discover that the removal of some impediment to investment or production is the prime requirement for getting a particular industry moving along the plan path. Similarly, it may find the contact with private firms an effective way of bringing to their notice, in a timely manner, investment and production opportunities (in conformity with plan needs) of which they might otherwise not be aware.

Some practical problems of consulting with the private sector

While, in principle, the desirability of consultation is recognized in virtually all the developing countries that have engaged in planning, the making of practical arrangements to permit the required dialogue has proved to be a difficult matter. And where machinery has been created for the purpose, it has not always provided the necessary contacts at the appropriate level and at the critical times. Even if, as suggested above, the bulk of the economy can be ignored as far as the establishment of formal machinery is concerned, the needs remain multiple; consequently, a single institutional point of contact is likely to be quite inadequate. On the other hand, the multiplication of committees to deal at various levels with the problems arising in the key areas soon makes the planning machinery too cumbersome to be effective within the rather strict time schedules necessary for formulating and implementing the normal medium-term (five-year) plan. Experience suggests that a more pragmatic approach is needed so that the essential strategic links between government and private producers can be forged with the minimum of institutional complication.

The essential links are those that can assist in determining objectives and following up on performance in the case of industries in which a lag would be particularly damaging to the plan as a whole. The list of such industries differs from country to country but, in general, it would include power, cement and steel, construction and civil engineering, the main means of transport, the leading exports and the basic food-stuffs. The links would have to be at both the technical level and the business investment-decision-making level, and at both levels care would need to be taken that, wherever there was a potential divergence of interest between management and labour, both sides were involved in the consultation process.

If standing industry committees are created, they would need to be manned by persons of comparable technical status: no meaningful dialogue can be expected if the disparity between the participants is too wide. If, for example, the official representatives are drawn from too low an echelon of the civil service, or lack the essential expertise, they may not be taken seriously by private industry, or even worse, they may be talked into recommending measures which are unnecessarily generous to sectional interests. On the other hand, few Governments in the developing countries are so well staffed that they can afford to commit senior civil servants to frequent or lengthy meetings with the representatives of private industry. The shortage of personnel with the technical, managerial or business qualifications necessary to engage in economic planning in co-operation with private entrepreneurs remains a major handicap in most developing countries.

The size and mode of operation of such committees depend in each case on the organization of the particular industry whose integration into the planning process is required. In most developing countries, the key industries comprise very few separate firms and, in general, representation of each of them might be quite practical. In some cases, the committee might be the forum in which arrangements were actually made for the desired expansion in capacity, in others it would provide merely a test of feasibility, an indication of which other actions were required to ensure the desired growth and, subsequently, a reviewing post for assessing performance and, if necessary, for adjusting targets and modifying policies. In connexion with this function of regular review, such committees might serve a valuable purpose in providing or helping to gather the relevant data regarding investment and production, both recent actual and future intended.

In so far as the main exports are agricultural in origin, special arrangements need to be made. These would involve consultation between the planning authorities and the department of agriculture, in the first instance, and then between the latter and the farmers, through co-operatives, or other farmers' organizations or extension services. Agricultural banks and other credit services may also have to be brought in since the problem of financing increased production is likely to loom large in most developing countries. Similar arrangements would be necessary in respect of the principal food crops, which would also rank as key products for purposes of the plan.

Larger and more widely representative bodies, such as chambers of industries and commerce and trade union federations, would act in part in a general advisory capacity both in respect to the over-all pattern of development objectives and in respect to the use of various policy instruments. They may also play an important part as liaison with the population at large and in generating enthusiasm among the business community—and especially those indirectly involved in the industrial and agricultural sectors—for speeding up economic growth in general and for helping to implement the plan in particular. The Committee for National Guidance, a joint public-private organ, created by the Ministry of Planning in the United Arab Republic seems to have served this purpose (see table 4). In India, there is a National Advisory Committee which has made great efforts to disseminate informa-

Table 4. Machinery for integrating the private sector into the planning process in selected developing countries[a]

Country	*Participation in formulation*[b]	*Implementation and review*	*Public information*
China (Taiwan)	1. Advisory Committee on the Plan 2. *Ad hoc* working groups on the agricultural plan	Provincial governments with representatives of private sectors and ministries	1. Consultative committee of sector leaders 2. Investment guidance by Council for International Economic Co-operation and Development
India	1. Development councils for certain industries 2. Working parties of the Planning Commission 3. General consultation with business and trade union groups	Indirectly through development councils	1. National Advisory Committee on Public Co-operation 2. Planning forums (950 in 1964) 3. Central Institute for Research and Training in Public Co-operation
Pakistan	*Ad hoc* consultation by Planning Commission	None	Government's use of mass media of communication
Turkey	None	None	State Planning Organization in co-operation with the Union of Chambers of Commerce
United Arab Republic	Consultative committees	Progress reports required from individual firms	Committee for National Guidance uses mass communications media
Venezuela	1. Informal dialogue between Planning Commission and representatives of business (FEDECAMARAS) 2. Consultation through *ad hoc* advisory councils	None	1. Government-sponsored lectures 2. Public meetings organized by FEDECAMARAS

Source: Centre for Developing Planning, Projections and Policies of the United Nations Secretariat, based on *Planning for Economic Development: vol. II—Studies of National Planning Experience* (United Nations publication, Sales No.: 65.II.B.3); *World Economic Survey, 1964: Part I—Development Plans: Appraisal of Targets and Progress in Developing Countries* (United Nations publication, Sales No.: 65.II.C.1); *Economic Bulletin for Latin America*, vol. VIII, No. 2 (United Nations publication, Sales No.: 64.II.G.1); India, *Fourth Five-Year Plan—A Draft Outline* (New Delhi, 1966); Turkey, *First Five-Year Development Plan, 1965 Annual Programme* (Ankara, December 1964); Pakistan, *The Third Five-Year Plan* (Dacca, 1965); China (Taiwan), *Council for International Economic Co-operation and Development, Republic of China, Organization and Function* (Taipeh, 1964); Pedro R. Tinoco Lyo, "Participación del sector privado en la planificación venezolana", paper presented at meeting of Interplan, November 1966, Caracas.

[a] Based on most recent plan.

[b] Including target setting, engaged in to a varying extent in all the countries listed.

tion about the plan, though so far with disappointing results if mass awareness is taken as a criterion.

Some countries have experimented with larger and more representative bodies for individual industries, such as the development councils that have existed in India since 1951. While these have been useful both for making the industry "development-conscious" and for communicating ideas (and complaints) to the Government, they have not been used extensively or proved very helpful in formulating or implementing particular plans.

At the other end of the scale, special arrangements usually have to be made when the desired development is not the expansion of existing capacity but the establishment of a new industry. Here the Government may have to conduct a series of *ad hoc* bilateral explorations with domestic enterprises in allied fields that might be interested and equipped to undertake the new venture, or call in foreign consultants or open up discussions with foreign companies in the industry in question. Such arrangements may give rise to a more permanent consultative committee to watch over the progress of the new industry, but in the first instance the main preoccupation of such a committee is more likely to be negotiation of questions of size and technology and of the terms on which the investment is to be made—access to inputs, government participation, protection, tax liability and so on.

The problem of keeping developments under review as the plan is implemented has proved one of the most difficult. On the whole, the organs established to help in formulating investment plans and production targets have not been successful in keeping track of subsequent progress so that emerging imbalances could be averted or objectives modified in the light of actual events and achievements. There has been a notable deficiency in the flow of relevant information to the authorities responsible for administering the plan. The result has often been poor resource allocation, as, for instance, when additional investment is encouraged in areas in which existing capacity is being seriously under-used. The reluctance of businessmen to divulge information and the difficulties experienced by Governments in administering up-to-date statistical services should not be allowed to rule out the gathering of certain key measurements of performance on which rational policies for implementing—or modifying—the plan must be based.

Once a satisfactory rapport has been established between the planning authorities and the entrepreneurs concerned, it should be possible to ensure regular current reporting on capacity, output, investment intentions and actual or incipient input bottle-necks or any other factor which appears to be hampering progress along the planned lines. Such information would be for the exclusive use of the planning authorities and would not be passed on to other arms of government. If it is published in due course it would be subject to the restraints that are customarily written into legislation governing statistics: the data would be processed to the point at which they would no longer reveal the facts relating to individually identifiable concerns.

It is clear that the required rapport cannot be established in the absence of confidence. The basis of such confidence is the Government's efficiency in carrying out the public sector programme and its firm handling of the economy as a whole. Since in this matter each success makes the next one that much easier to attain, it is better to begin the planning process in a modest way than to invite failure by being unrealistically ambitious in scope or targets.

It is also clear that no general prescription can be laid down with regard to the mechanisms through which the Government can best conduct the necessary dialogue with private producers. Much depends on the structure of the economy. Here too, realism is likely to pay off. In most developing countries, the capacity of the civil service is the limiting factor, and it is usually considerably less in the technical and managerial fields than it is in the office in which paper plans are drawn up. Elaborate machinery appropriate for a country with a diversified economy and a competent and sophisticated public administration would be quite out of place in most developing countries.

Among the countries that have been planning for some years there has been a good deal of experimentation and more will obviously be needed. The records so far thus contains some marked differences in approach and in organization, reflecting differences not only in economic structure and in the comprehensiveness of the plan but also in Governments' conception of their relationship with the private sector. In Turkey, for example, no attempt has been made to consult farmers on their role in the plan; in China (Taiwan), by contrast, no less than seven working groups were assembled to formulate the main aspects of the most recent (1964-1967) agricultural four-year plan, and this was followed up by review and performance machinery based on village officers, farmers' associations and irrigation organizations. In the United Arab Republic, where much of industry is in government hands, consultation with private firms is done through a Joint Committee for Planning which has six consultative committees and no less than sixty subcommittees; by contrast, in Pakistan, where recent progress has been ascribed largely to the responsiveness of the private sector, the "industrial investment schedules" which set priorities and targets are worked out very largely by government agencies which merely invite the participation of representatives of private industry.

In countries with a small industrial base and a rudimentary capital market, the need for consultation machinery may not be urgent; the Government may be able to exercise the required degree of leverage through a development corporation, provided the latter's promotion and lending policies are attuned to the plan. Similarly, agricultural development among peasant producers may be kept in line by appropriate policies pursued by official marketing boards, combined where necessary with the extension services of the Government's agricultural department; it may be too difficult to organize additional machinery with much hope of success. Given the scarcity of administrative skills in most developing countries, there would seem to be every reason to start by harnessing existing machinery to plan purposes, setting up new bodies only when the need has been clearly demonstrated. And when new mechanisms are created, it is towards the strategic segments of the economy—where bottle-necks may occur—that they need to be first directed.

THE MEANS FOR INFLUENCING THE PRIVATE SECTOR

In so far as the investment and production policies spontaneously pursued by the private sector are not, or are considered not likely to be, in conformity with the plan, the Government may find it necessary to try to influence the behaviour of the industries that are out of line. The authorities have at their disposal a wide range of instruments for this purpose: they extend all the way from the offer of marginal incentives to undertaking the required investment or production themselves.

In choosing the instrument it will use, the Government has to keep in mind not only probable effectiveness and ease of application—a form of benefit-cost appraisal—but also the extent to which the instrument in question is being used, or is likely to be used, for purposes other than plan implementation which may require other types of action, possibly conflicting with that dictated by the plan. It also has to keep in mind the whole range of instruments in order to maximize their combined impact or at least to ensure that the inconsistencies are reduced to a tolerable minimum. It must adopt a broader approach than it can expect of the industry whose actions it is seeking to influence: it has to consider the whole pattern of its relations with the private sector, both current and future, aiming always to establish a climate in which individual enterprises—management and labour—can more readily identify their own interests with the development of the economy as a whole.

As in the case of consultation machinery, the means of influencing the private sector have to be selected in the light of the requirements of the particular economy; though there are some lessons to be learned from experience elsewhere, there are no generally applicable formulae. While direct measures have usually proved more immediately effective, indirect measures have distinct advantages in an economy in which market mechanisms are working fairly smoothly. While physical controls have an immediate direct impact, they pose serious problems of administration and co-ordination, and lend themselves to an arbitrariness which can be very damaging in the longer run. On the other hand, fiscal measures have often proved weak as incentives, even where they have worked efficiently as deterrents. And in all cases, the cost of deploying the instrument has to be taken into account not only in the conventional administrative sense but also in such things as the revenue forgone in a tax or tariff concession, the foreign exchange committed in an import permit or the inflationary effect of a line of credit.

Although the use of the various instruments to stimulate economic development in a general way has been widespread over the post-war period, there has been relatively little experience in their more delicate, selective and purposeful deployment as an adjunct of a particular plan. Where this has been attempted, the difficulties have been less a reflection of the problems of using a specific instrument than of conforming the use of other instruments so that a logically consistent "package" of influences is brought to bear on the economy to give it the desired shape. For purposes of use by the planning authorities, however, such a distinction has to be made with great caution. From a practical point of view, the various policy instruments are administered by different agencies of government whose efficiency, flexibility and willingness to co-operate with the planning authorities may often be far from uniform. Administrative convenience cannot be allowed to determine the choice of instrument. For not only do the terms of access affect the price of the factors—and hence the cost and profitability of business—but the essential problem facing the planner in his search for the means of guiding or influencing the private sector concerns the simultaneous deployment of the various instruments and not the efficiency of any one used in isolation.

Instruments affecting the profitability of business

The most widely used instrument affecting profitability is the fiscal system, particularly the taxation of income. Differential tax rates have long been imposed not only in the light of their revenue-raising potential but also with a view to encouraging or discouraging various activities. Agricultural incomes have been taxed more lightly than industrial incomes, new industries have been taxed more lightly than old industries, favourable rates have been applied to certain types of industries, to industries in particular localities, to domestic shareholders (as compared with foreign shareholders), to mines working low-grade ore (as against high-grade) and so on. At the extreme, "tax holidays" have been granted, sometimes for periods of several years—as long as ten years in some cases—as a means of attracting new industries or even new concerns.

Similar differentials have been applied to investment. By permitting approved forms of capital expenditure to be written down more rapidly than others or, more commonly, by granting preferred industries special investment credits, the expansion of an established firm or the establishment of a new one has been made more attractive to the entrepreneur than it would otherwise have been.

Relative profitability has also been affected through the customs tariff. New industries have been attracted by the offer of protection, enabling them to raise the prices of their products above the world market level. Selected industries have also been assisted by remission of duties on imported inputs, particularly plant and equipment and in some cases even components.

Countries with multiple exchange rates have manipulated such rates to achieve a similar purpose. Favourable exchange rates have been accorded weak or new export industries, while traditional and stronger industries have had to surrender their foreign exchange earnings on a less favourable basis. Import rates have also been varied to facilitate or discourage particular imports.

Internal prices have also been subjected to more direct control. Higher than market prices have been offered to stimulate production in certain industries including, in some countries, selected farm crops. Price ceilings have also been imposed, usually to protect consumers, but frequently affecting the profitability and ultimately the output and expansion of the industries concerned, thus limiting the protection to those who are able to obtain supplies. As a result, price controls as such have rarely achieved their intended purpose without the use of other instruments: the repudiation of price as a distributive device has made it necessary to introduce alternative means of allocating the available supply, so that the administration of price has usually been accompanied by rationing or other physical controls over allocation.

Even a cursory examination of the use the developing countries have made of these instruments shows that while they have often been consciously deployed in the general interest of economic development, there have been relatively few cases of close alignment between the way in which fiscal, exchange or price policies have been used and the precise objectives of the plan. Even in India, for example, where planning is fairly detailed and has a relatively long history, revenue needs have usually taken precedence over the use of fiscal incentives to achieve specific plan targets. And where fiscal incentives have been used, they have tended to be general rather than discriminatory. Thus the exemption from taxes that is granted on earnings up to 6 per cent of capital is not a selective one; all new manufacturing undertakings and hotels (employing power or more than twenty workers) are eligible. In most developing countries, the extent of discrimination in the use of such instruments has been limited to a broad attempt to encourage industrial investment or diversification. There are very few examples of a carefully tailored set of incentives and deterrents designed to influence the private sector along well-defined paths in conformity with the plan. Often the fiscal and tariff policies in question have ante-dated the plan and have been more or less unaffected by it. In many cases, moreover, the instruments have been deployed for other purposes—price controls for holding down consumer prices, exchange rates for saving foreign exchange, duties and taxes for increasing government revenue—not necessarily in conformity with the plan, and sometimes not wholly consistent with one another.

Failure of Indian cement production to expand at the planned rate in recent years has been ascribed in part to the system of price control and distribution designed in the interest of other forms of investment in which cement is an essential input. The decontrol of the cement industry in January 1966—opening up the non-government segment of the market—was intended to permit an increase in profitability and hence in capacity. Where price stability and the expansion of output are not consistent simultaneous objectives, a policy choice is unavoidable: what has to be sought is the least disruptive way of carrying it out, with the over-all purposes of the plan in view.

While consistency in the way in which the various means of affecting profit are used at any one time is an obviously desirable goal, it has to be borne in mind that they are not equally effective in their several purposes. Hence failure to deploy them in a consistent and purposeful manner may not always be as serious in practice as it is in principle. For some of the instruments have proved rather weak in accomplishing their ostensible purpose. "Tax holidays" and rebates, for example, seem to have exercised relatively little influence on the decisions of entrepreneurs. Where tax rates are low and administration loose, the advantage of remission may be rather small, and possibly offset, at least in the case of small and medium-sized firms, if to qualify for it the entrepreneur has to make special returns, disclose more information or is subject to a greater degree of surveillance. Market factors, the availability of appropriate inputs and confidence in the business climate are often far more influential than marginal tax differences.[2] Moreover, where the Government retains a discretionary right to determine eligibility, administrative formalities and delays may seriously detract from the value of the concession.[3]

On the whole, the tariff instrument has proved a more potent one than the tax instrument in influencing investment in new industries: lower cost inputs and protection from external competition are

[2] Cf. some of the surveys made in Central American countries. In Costa Rica, two thirds of the companies that had benefited from the local tax incentives in the 1950's indicated that the investment in question would have been made even without the incentive. See S. L. Schreiberg, "The U. S. private investor and the Central American Common Market", in United States Congress, Joint Committee on the Economic Report, *Latin American Development and Western Hemisphere Trade Hearings*, 89th Congress, September 1965, p. 272. Similar conclusions emerge from an inquiry in Mexico where, between 1951 and 1955, out of 150 cases in which tax exemption has been denied, not one was deterred from going ahead with the intended investment. See S. G. Ross and J. B. Christensen, *Tax Incentives for Industry in Mexico* (Cambridge, Massachusetts, Harvard University Press, 1959), p. 101.

[3] In Ghana, during the 1950's, it took from nine to twelve months to settle applications (J. Harvey Perry, "Taxation and economic development in Ghana", a report prepared for the Government of Ghana (TAO/GHA/4/Rev.1), pp. 43-45). Even longer delays—up to two years in some cases—are reported in Mexico.

more fundamental advantages than relief from certain tax obligations. While achieving a greater result, however, tariff adjustment—whether downward to reduce cost or upward to increase protection—often involves a more serious cost. Tax exemption denies the Government certain revenue, but usually only temporarily—recent concessions have been made for two to five years in Malaysia and Nigeria, two to six years in Pakistan, five years in Sierra Leone, five to ten years in Ghana, ten years in Uruguay, ten to fifteen years in Chad—and only as a prelude to an expansion of taxable capacity if the new concern so benefited actually succeeds. Tariff adjustments in favour of particular industries may also involve a loss of revenue, at least in so far as they reduce the duty payable or fulfil their ostensible purpose of excluding imports. Potentially more significant, however, is the fact that they introduce a risk for the economy as a whole of raising the cost structure to the particular detriment of export activities.

As in the case of fiscal incentives, the tariff instrument has been used only rarely for the specific purpose of implementing a plan. Its deployment has almost invariably been connected with a general development strategy based on import substitution. This has been particularly true in Latin America and is one of the reasons for the high tariffs which characterize this region (see table 5). High rates of duty have in turn contributed to higher internal costs and thus accentuated the difficulties experienced by many of its export industries.

Table 5. Average rates of duty applicable in selected Latin American countries compared with common external tariff of the European Economic Community, 1963[a]

(Percentage of f.o.b. value)

Category of product	*Argentina*	*Brazil*	*Chile*	*Colombia*	*Ecuador*	*Mexico*	*Paraguay*	*Peru*	*EEC*
Primary commodities and capital goods (51 products)	96	134	58	64	35	32	69	18	13
Non-processed food-stuffs (13 products)	123	264	46	185	37	65	99	21	21
Industrial raw materials (10 products)	55	106	111	57	52	38	63	20	1
Capital goods (28 products)	98	84	45	18	27	14	57	16	13
Semi-manufactured and durable consumer goods (43 products)	139	143	96	48	56	58	84	25	10
Durable consumer goods (11 products)	266	328	90	108	80	147	104	30	19
Intermediate products (including fuels), for use in durable consumer goods industries (32 products)	95	80	98	28	48	28	77	23	7
Non-durable consumer manufactures (31 products)	176	260	328	247	117	114	77	72	17
Processed foods (14 products)	192	280	436	359	145	110	76	41	19
Other non-durable goods, including semi-processed products (17 products)	163	244	239	154	76	117	78	98	15
Over-all average (125 products)	131	168	138	112	62	61	76	34	13

Source: Centre for Development Planning, Projections and Policies of the United Nations Secretariat, based on *Economic Bulletin for Latin America*, vol. IX, No. 1, March 1964 (United Nations publication, Sales No.: 64.II.G.8), p. 75.

[a] The figures represent simple arithmetic averages of customs duties (plus other customs charges where applicable) expressed in *ad valorem* terms.

The use of the tariff instrument for plan implementation implies a much more discriminatory process. Not only would its use be confined to a relatively few industries, judged to be in need of the stimulation for the attainment of planned output, but its choice as the stimulant would be confined to those industries with reasonable expectations of becoming viable (by global standards) in a foreseeable time. This would also imply some follow-up or review mechanism for assessing the progress of the protected industry both in terms of the output objectives of the plan and in terms of productivity and cost. Manipulation of customs duties would also need to be supported by an appropriate policy regarding rates of exchange: the more a tariff is required to compensate for an over-valued currency, the more difficult is it likely to be to use it discriminatingly as a policy instrument for purposes of plan implementation.

Perhaps the most serious difficulty in using indirect measures to call forth a desired sequence of actions from the private sector lies in the fact that in many developing countries entrepreneurs are not very sensitive to small signals: where risks are high and the rewards of success large, the power to influence decisions by means of conventional policy instruments is correspondingly weak. This is particularly the case in an inflationary environment, in which nothing short of direct measures involving physical controls or official participation in production may be found capable of exerting the requisite pressure on the private sector. The significance of this relative insensitivity is increased by the fact that time is itself a critical element in any phased programme of economic development. Not only is there an interdependence among the various components of the plan, one activity rushing in with the next, but the whole plan period may itself be a short one in relation to the changes that are to be brought about. In most developing countries the industrial base is small, and by that standard the investment decisions the private sector is called upon to make may often be of major dimensions. In those circumstances, moreover, there may be a long lag—much longer than in an industrially advanced country—before such a decision bears fruit in increased output. It is clear that the purposeful deployment of indirect incentives and deterrents as an adjunct to a plan is an intricate matter requiring a careful selection of policy instruments, their bold and firm application and their consistent support by other government action.

Instruments controlling access to scarce factors

Perhaps because planning itself is essentially a problem in resource allocation, in most of the developing countries with plans that are at all comprehensive, direct means of control have been used more frequently than indirect means to guide the economy in designated directions or to help achieve specific production or investment targets. The choice of instruments has also been influenced by the fact that some of the countries that have been experimenting with plans which embrace the private sector have been among those most notably affected with particular resource shortages judged to require rationing by means other than price. Thus physical controls have been set up not only over imports, foreign exchange, capital issues and access to credit but also over scarce commodities, particularly producer goods such as steel and cement, but in some instances also consumer goods such as food-grains. And over the whole network of direct controls there has been superimposed, in some cases, a system of industrial licensing under which all new fixed capital investment requires official permission.

As instruments of plan implementation, such direct controls suffer chiefly from the defects of their advantages. They are powerful and definitive in their impact. By eliminating, to a large extent, the judgement of entrepreneurs reacting to indirect incentives and deterrents, they impose a much greater burden of responsibility on the administering authorities not only for the broad direction and intent of policy but also for detailed decisions regarding investment, right down to the plant level. Such controls tend to be much more effective in preventing investment than in inducing it. Each control is a potential veto on action, whereas even if an appropriate share of every one of a series of scarce and rationed resources is allotted to an applicant, the result may still not be the creation of new capacity, if the market or the climate is judged unfavourable.[4]

Most developing countries have found it difficult to administer efficiently a system of direct controls. The ministries or departments which allocate the scarce resources are put in a position of great power and, at the same time, of great vulnerability as arbiters of private-sector investment. Co-ordination of their actions, both in terms of the criteria for allocation—namely, the objectives of the plan—and in terms of the sequence and timeliness of their decisions, has often been very poor, especially when the relative scarcity of particular factors has been subject to unexpected change. Indeed, even more than in the case of the indirect policy instruments, the direct controls have had to be deployed for purposes other than plan implementation. Thus, when poor crops or lower export prices have reduced the supply of railway wagons or foreign exchange available for allocation, it has proved difficult to distribute the cuts in allotments in ways that will contribute best to the fulfilment of plan intentions. Attempts to use objective criteria, such as historical shares, for the allocation of a scarce resource may seem fairer than more arbitrary methods and also relieve the administrators of awkward decisions, but in practice they have proved inefficient and quite out of line with plan needs which often require a deliberate departure from previous patterns.

Problems of co-ordination and promptness multiply as the number of control points increases. In Pakistan in 1963, no less than eighty permits had to be obtained from various government departments before a new industrial investment could be made.[5] In India, a committee investigating the operation of controls reported that it took two to thirteen months for the application for permission to make a new investment to be processed, and three fourths of the applicants in the sample studied by the com-

[4] In 1962 in India, 814 licences that had been granted for new investment in fifty-four different industries were revoked because the applicants had not acted on them. It is thought that some of these applications had been made by established interests merely to prevent potential competitors from acquiring access to the resources necessary for entering the industry in question. Cf. A. H. Hanson, *The Process of Planning: A Study of India's Five-Year Plans, 1950-1964.*

[5] Mahbub ul Haq, "Rationale of government controls and policies in Pakistan", *Pakistan Economic Journal,* March 1963 (Dacca).

mittee had to wait more than five months.[6] These are long delays in the perspective of a five-year plan.

Some of the complications are inherent in the very need for rationing. Whatever their nominal value, the market value of some of the scarce factors may be extremely high: there is thus a powerful incentive for entrepreneurs to try to obtain the largest possible allocation by applying for import permits, for example, or allotments of foreign exchange without proper concern about real costs. The resultant distribution—if not strictly guided by plan priorities and economic criteria—may make for an undue dispersion of the scarce factor and hence industrial units that are sub-optimum in size and profitable only behind the shelter of the import and exchange controls.[7]

On the other hand, the high real value of foreign exchange has made it a powerful instrument for rewarding behaviour conforming to the plan. Relating the foreign exchange allocation of an enterprise to its export performance, for example, has proved a strong incentive in a number of developing countries, capable of more subtle manipulation than a system of multiple exchange rates. Leaving specified proportions of such foreign exchange in the hands of the exporters has usually resulted in an increase in the sort of imports which, because they have not previously ranked for exchange allotments, yield high prices and profits on the local market. This is acceptable if it reflects a genuine increment in production and exports that would not otherwise have occurred; if it is merely the result of a diversion of supplies, plan priorities are almost bound to suffer.

Control over credit is also a potent means of influencing private investment, though in most developing countries it has been rather less effective than control over foreign exchange. As in the case of the other instruments, the provision of finance has been used much more often as part of a general economic development policy than as a designated means of ensuring or hastening the attainment of particular plan targets. In many developing countries, the principal institutions through which financial resources have been made available to the private sector were established well before any attempt was made at planning the economy, though in many cases they were associated with specific development strategies—the encouragement of industrial diversification through officially sponsored development corporations, or industrial banks, for example.

In some cases, the bank's charter has delimited the area of operation: the Industrial Bank of Turkey may lend only to certain specified high-priority industries, for example; the Banco Nacional de Desinvolvimento Economico of Brazil is concerned mainly with transport, power and basic industries (in that order) while the portfolio of the Agricultural, Industrial and Real Estate Credit Bank of Lebanon is to be divided in specified proportions among agriculture, industry and tourism. In other cases, the early involvement of a bank with a particular industry has tended to persist—as in the case of the Industrial Finance Corporation of India with the sugar industry, which accounted for almost a fourth of its advances in mid-1964—irrespective of the status of that industry in the priorities of the plan.

Though the post-war proliferation of financial institutions in the developing countries has coincided with the spread of interest in planning, few of the organs even among the publicly owned have been conceived of merely as the financial arm of the plan (see table 6). At best, their lending policies have reflected the general development intent of the plan; seldom have they limited their financing operations to the industries for which investment or production targets have been designated. Even where they have been designed to provide incentives to particular branches of production (by supplying credit not otherwise available or available only on more onerous terms) they have rarely abandoned their banking criteria for loans: the credit-worthiness of applicants has continued to be judged more by the probable profitability of the project itself than by its strategic importance in the complex of new investments contemplated in the plan. Private institutions have understandably applied banking standards even more strictly than have public ones.

Nevertheless, some financing operations have been closely identified with the plan. In France, for example, the Fonds de développement économique et social lends only for projects negotiated with the Ministries of Finance and Industry, and even the older Crédit national requires projects to be submitted first to the Commissariat du Plan. In the United Arab Republic, there are also banking institutions that act as financing arms of the planning authorities. And in 1964, India set up a special Development Assistance Fund, administered by the Industrial Development Bank of India, to help finance plan projects which for one reason or another—size, long maturation or low prospective return, for example—could not obtain resources from other institutions.

[6] See A. H. Hanson, *The Process of Planning: A Study of India's Five-Year Plans, 1950-1964,* citing the *Eastern Economist* of January 1964.

[7] Especially if the control authorities are subject to regional pressures. Cf. J. Bhagwati, "Economics of scale, distribution of industry and programming", *The Economic Weekly,* 1 September 1962 (Bombay).

Table 6. Main institutions helping to finance development plans in selected countries

Country	*Name of institution*	*Year of establishment*	*Ownership*	*Type of credit*	*Remarks*
India	Industrial Finance Corporation (IFC)	1948	51% public	All types	Between 1948 and 1964 it financed projects accounting for about 30% of net investment in the private sector
	State Finance Corporation	1953	51% public	Loans, guarantees	Loans up to 20 years. Preferred investment: "key" industries
	Industrial Credit and Investment Corporation (ICICI)	1955	Private	Loans (including foreign currency), equity, underwriting	Preferred investment: heavy industries
	Life Insurance Corporation (LIC)	1956	Public	Equity, underwriting	
	Industrial Development Bank (IDBI)	1964	Public	All types	Preferred investment: "key" industries, new projects
Israel	Industrial Development Bank of Israel (IDBI)	1957	26% public	All types	Between 1958 and 1964 it financed 40% of net industrial investment in Israel
Pakistan	Pakistan Industrial Development Corporation (PIDC)	1952	72% public		Preferred investment: heavy engineering, chemicals
	Pakistan Industrial Credit and Investment Corporation (PICIC)	1957	Private	Loans, guarantees and underwriting	
	Industrial Development Bank (IDB)	1961	51% public	Loans, guarantees and underwriting	Preferred investment: small and medium-sized industries of schedule I of development plan
Turkey	Industrial Development Bank of Turkey (IDB)	1950	Private	Loans (including foreign currency) and equity	
United Arab Republic	Egyptian Industrial Development Bank		Majority public	Loans and equity	Preferred investment: small industries
Venezuela	Venezuelan Development Corporation (CVF)	1946	Public	Loans and equity	Preferred investment: industries earning foreign exchange, users of domestic raw materials
	Corporación Financiera Venezolana de Desarrollo	1963	16% public	Loans (up to 10 years), equity and guarantees	

Source: Centre for Development Planning, Projections and Policies of the United Nations Secretariat, based on Business International Corporation, *Financing Foreign Operations* (New York, 1966), Business International Corporation, *Industry, Licensing and Trading Conditions Abroad* (New York, 1965), Antonin Basch, *Financing Economic Development* (New York, Macmillan, 1964), Shirley Boskey, *Problems and Practices of Development Banks* (Baltimore, Johns Hopkins Press, 1964, 3rd printing).

The influence that the Government is able to bring to bear on the private sector through financial institutions is chiefly through the availability of credit rather than through the terms on which it is offered: the latter have not been notably discriminatory among sectors, and though the institutions in question have generally charged rates of interest competitive with, and even somewhat below, those of the conventional sources of funds, the evidence suggests that the cost of the credit has been a secondary consideration among borrowers in most developing countries, especially where inflationary pressures have been strong. Moreover, even the offer of credit is not a uniformly potent instrument. It is likely to have much more influence on new enterprises, for example, than on established concerns, which not only have readier access to banks and other regular financial sources but also are generally able to finance much of their expansion from internally generated funds. The growth of such concerns is affected much more by fiscal policy, investment "climate" and other determinants of profitability.

The purposeful use of the credit instrument to facilitate plan implementation, therefore, requires not only the provision of finance on appropriately differentiated terms but also the means of controlling, or at least influencing, other sources of credit.[8] The more liquid the economy, the less effective is a financial incentive likely to be. By the same token, the better organized the local capital market, the less influence is a given financial intermediary likely to wield. Special institutions have tended to be most useful in developing countries seeking to achieve non-inflationary growth in the face of an inadequate rate of saving and a rudimentary capital market. They have been particularly welcome when they have been able to make foreign currency loans, and the International Bank for Reconstruction and Development has found them a convenient means of chanelling credit to productive enterprises on a scale too small for its regular government transactions. In such circumstances, institutions that have no direct connexions with the plan can easily be harnessed to plan purposes on an *ad hoc* basis of individual investments.

STRATEGY FOR PLAN IMPLEMENTATION IN THE PRIVATE SECTOR

The foregoing review of the relationship of the private sector to an official development plan and of the means at the disposal of a Government to influence private entrepreneurs to act in conformity with such a plan suggests the essential elements of a strategy that might be followed in implementing plans that involve the private sector in a material way.

The essential preliminary would be the identification of those portions of the private sector in which specific structural changes or the achievement of designated investment or production goals (or both) are indispensable to the fulfilment of the plan. No less important would be the removal of as many as possible of the recognized impediments obstructing the desired behaviour on the part of the entrepreneurs in question. At some stage during the formulation process—certainly before finalization of the plan—would come the setting up of appropriate machinery through which a dialogue could be maintained between the Government and each of the key components of the private sector.

Once the plan was formulated, one of the main objectives of the Government in such dialogues would be to facilitate spontaneous action in the key industries that would accord with the needs of the plan. In so far as the prospective growth and change in demand postulated in the plan were insufficient to evoke anticipatory action, the Government would face a fourth problem, namely, to devise a suitable combination of policy measures to induce the desired pattern of behaviour. In selecting the policy package, the Government would have to bear in mind not only the need for internal consistency and for minimizing real cost but also the possibility that in the course of the plan period the policy instruments in question may have to be deployed for other purposes. Among these, most developing countries are likely to find that the most frequent is that of managing the economy during periods of short-term disturbances. At such times the conflict between stability and growth tends to be at its sharpest, and the problem takes the form of using the instruments to meet immediate needs with the least detriment to longer-term targets and to the strategy by which the private sector is being directed towards their achievement.

Key elements in the private sector

The particular segments of the private sector for which special arrangements have to be made if they are to develop along lines postulated in a plan differ from one country to another, depending partly on the structure of the economy and partly on the extent to which the Government is able to exercise control over the elements in question by virtue either of laws and regulations or of participation in ownership. The critical elements are those in which failure to achieve a scheduled expansion in capacity or output is likely to jeopardize the achievements in other sectors and even the plan as a whole.

---

[8] For a case study of the problems of allocating credit in the interest of a development policy, see R. L. Bennet, *The Financial Sector and Economic Development: The Mexican Case* (Baltimore, Johns Hopkins Press, 1964).

In most developing countries the list would include, in so far as they are in private hands, power and transport and other areas of infrastructure on which the performance of industry and agriculture depends. It would include the production of basic food-stuffs for the market, and major local industries whose output is to be used in the planned programme of investment. It would include new industries planned as "growing points" in particular regions of the economy. And it would include at least the leading export activities and, if the external market prospects for these are unfavourable, some of the less important export activities and even the producers of new types of exports. In general, the Government's concern would be for the potential bottle-necks of any consequence—industries and activities whose lag or failure might have serious repercussions on other parts of the economy as it is expected to develop in the light of the Government's own investment intentions.

Among the strategic elements thus identified, priorities can be assigned partly on the basis of an assessment of the possible secondary effects of a lag or failure and partly on the basis of the probability of such difficulties. The "difficult" segments of the economy in this sense are those in which the required investment is large by local standards, those in which there is likely to be a long delay before the investment yields the required output, those in which the desired expansion in output is contingent upon institutional changes or other forms of reorganization, those in which ownership and control are so dispersed that the activity cannot be harnessed to the plan in matters of motivation and decision making and in some cases, those in which ownership is in foreign hands.

In some ways these strategic "problem" segments set the limits for the plan. If the plan is not to be unduly circumscribed, optimum goals need to be set for such segments—goals that are as ambitious as possible, yet feasible and attainable. Goals of this nature can be set only in consultation with the decision makers of the segments in question. It is at this point in plan formulation that consultation with the relevant elements of the private sector needs to be organized. The machinery devised for such consultation should be capable of regular use throughout the plan, keeping under review the progress of the segment concerned and ready to recommend changes in methods or policies should lags or imbalances begin to emerge.

The nature and amount of such machinery will be determined by prevailing circumstances. As indicated earlier in this report, most developing countries are poorly equipped to administer elaborate consultative mechanisms. In the case of the strategic elements, however, it seems unrealistic to expect the private sector to behave in conformity with the plan unless appropriate steps are taken to ensure that the targets are reasonable and the producers fully aware of the essentials of the plan and of their role in it. It is for the Government to work down the list of principal problem segments, organizing the means for consultation and review for as many of them as seems practicable.

The content of the plan should reflect the results of such consultation. This is particularly necessary where structural changes are found to be called for. Resettlement of peasants, consolidation of land holdings and other tenure changes of this nature may be required in order to attain reasonable targets in the agricultural sector, for example, and it is often sound policy to write such restructuring into the plan as one of the development objectives. The renegotiation of the terms on which mineral or other concessions are held may also be an appropriate subject for consultations in advance of the final formulation of the plan. Similarly, to attain one or other of the essential industrial goals—for steel production or fertilizer production, for example—it might prove necessary for the Government to enter into partnership with private producers, and such a joint venture might also be specified in the plan. If traditional exports seem unlikely to realize the required expansion in foreign exchange earnings, it might be necessary to stimulate secondary and minor export items or explore completely new products; the plan might well specify the intended action and methods, at least in general terms, as a distinct objective.

Realistic appraisals of the key segments are essential if the plan is to become a credible blueprint for action. The more credible it is, the more likely is the private sector to take appropriate decisions about investment and production on a purely voluntary, self-interest basis. Confidence between government and private sector will be raised and the task of administering the plan will be that much lighter. And the Government will have greater freedom to use its policy instruments for the general purposes of economic management.

Implementation problems in the agricultural sector

By far the most difficult sector to plan for in most developing countries is agriculture. Because of its central role in the economy, both as a source of income and as a source of supplies for consumers, for many processing industries and for sale abroad, agriculture cannot be allowed to lag if the over-all pace of economic development is to be accelerated. To plan for agricultural expansion, however, raises major problems in virtually every area of implementation, most notably in effecting necessary institutional and technological changes in circumstances which involve great strain on administration and logistics.

The institutional changes that are needed in order to make possible an adequate rise in agricultural output in the light of plan requirements tend to involve questions of tenure that are deeply embedded in tradition. At the one end of the scale they include the putting to beneficial use of land locked away in large estates. At the other end of the scale, they include the consolidation of uneconomically small holdings and the adaptation of communal tenure to permit the effective use of new inputs such as irrigation water, higher-yielding seed varieties, fertilizer or mechanical means of ploughing, harvesting or transporting supplies and produce. Changes of this nature are notoriously difficult to bring about. Not only are they usually resisted by established interests sceptical of the argument that development will be to their ultimate advantage too but they may in fact be counter-productive in the short run.

Implementation of such changes thus requires thorough preparation if the potentially disruptive effects are to be minimized. This calls for strenuous efforts in an area in which most developing countries are handicapped both by the political power wielded by those resisting change and by the many varied difficulties of administration at what is in many cases the periphery of the market economy. Among the tasks that are involved are the carrying out of cadastral surveys, the organization of demonstration farms to convince peasants, often illiterate and tradition-bound, that new techniques pay off the underwriting of the main risks of innovation, the resettlement of peasants and all that process entails in the way of housing and the provision of supplies and the arrangement of credit and the marketing of crops. These would be formidable assignments even to experienced cadres with a sure knowledge of the facts. In many cases they have been attempted in the face of a good deal of ignorance—both anthropological and agronomic—and by teams whose composition reflects the widespread reluctance of the ablest civil servants to live and serve in poor and backward areas.

Even where major institutional changes are not contemplated in the plan, keeping the agricultural sector in line with plan needs remains a task beset by difficulties. The geographical spread of the sector makes consultation heavily dependent on the extension services of the ministry of agriculture, and in very few countries are these a flourishing and well-supported part of government machinery. Instability of output, awkwardly high in many developing countries, tends to increase when, in the effort to expand production, the margin of cultivation is pushed outward: vulnerability to weather and other natural phenomena remains very great in most developing countries and a bad drought or flood or insect-infestation can so affect the supply of basic food-stuffs or a leading export that other plan targets are threatened. Thus the agricultural administration, almost everywhere, tends to be preoccupied by day-to-day emergencies and crises, ill-equipped to tackle the larger and longer-term problems of planned development.

Notwithstanding the manifold difficulties, it is clear that unless an adequate response is forthcoming from agriculture, no development plan can avoid potentially crippling imbalances. To elicit such a response from an atomistic peasant economy requires not only a considerable strengthening of the effort that has hitherto been devoted to the agricultural sector in most developing countries but also the pursuit of appropriate supporting policies in related fields, especially those affecting the supply of farming requisites and the distribution of farm products.

Recent experience suggests that the machinery for integrating the agricultural sector into the plan is likely to function best if it has a suitable geographical structure, based not on the political division of the country but as far as possible on agronomic similarities. Natural features such as rivers, so often used as convenient boundaries for provinces and districts on a political map, are likely to turn out to be major integrating factors for the purpose of agricultural administration. Within a relatively homogeneous agronomic region the essential substrata of factual information can more readily be established, optimum technologies worked out, suitably impressive experimental and demonstration farming conducted, a common attack on plant pests and diseases launched, appropriate arrangements made for crop financing, and transport facilities planned with a view to providing as many farmers as possible with access both to the new inputs required by the technological strategy that is being adopted and to the market for their crops, primary and subsidiary. The similarity of interests and needs within regions demarcated in this way tends to facilitate the organization of farmers for common purposes such as the improvement of infrastructure, the acquisition of inputs on the best terms, the erection of storage facilities and perhaps of processing plants and—not least, in the present context—to acquaint them with the plan, consult them about goals, disseminate productivity-raising knowledge and in general motivate them to contribute their best efforts towards achieving plan objectives.

The success of regional organization of this nature will depend to a large extent on the appropriateness and adequacy of the support received from the centre in collateral areas. Due priority has to be given to the needs of such regions when investment policies are determined in transport and industry. And price policy must reflect the importance of relating the reward of the farmer to his output in a sufficiently certain and generous manner to provide him with convincing tangible evidence of the advantages of a positive response to the urging of the planning authorities when they speak through the local agricultural administration.

The range and consistency of policies

One of the gains derived by government from effective consultation with the private sector is a more accurate appreciation of what policies and instruments are likely to yield the best results when encouragement or discouragement is required to keep particular segments of the economy in line with the plan. When new industries are to be established, indeed, the consultation may take the form of negotiation, with the Government offering certain concessions or privileges or exploring the possibility of its own involvement in order to induce the required investment. It was argued earlier in this study that the more effective the consultation, the better the rapport between government and private entrepreneur, the more credible the plan, and the more successful the Government was in keeping the economy stable and in reducing non-economic risks and uncertainities, the greater the probability of a spontaneous response to the plan.

In the circumstances prevailing in most developing countries, however, appropriate anticipatory action by private entrepreneurs cannot be relied on to keep the economy in line with the plan. The nature and magnitude of the changes that may be required in some areas and the risk that lags may occur in key sectors, altering the pattern of growth and impairing the planned balance, combine to make it necessary to deploy the various policy instruments discussed in the previous section specifically for plan purposes.

Thus, to an important degree, the art of plan implementation in the private sector lies in designing policy "packages" so that each of the specific development objectives is attained at the least possible cost to other parts of the economy. In general, this means pinpointing the factors preventing the desired development and then removing or counteracting them in the most efficient manner. This may involve the provision of credit, or assured access to the foreign exchange necessary to import plant or components not available locally, or protection from foreign competition during an initial high-cost phase of production, or the reduction of risk through a rapid writing down of capital charges, or a combination of such measures in optimum proportions. As the various instruments are often controlled by different branches of government, the formulation of an internally consistent package entails a special effort on the part of the planning authorities.

The difficulties that most developing countries have encountered in assembling a consistent set of measures for attaining a given plan objective lie in the fact that the government departments administering the instruments in question may in fact be pursuing other objectives—maximizing revenue, holding down the cost of living, conserving foreign exchange, liberalizing trade and so on. In pursuing the purposes of the plan by seeking to induce certain changes in the private sector, the Government is rarely able to abandon the other objectives; they are determined by fiscal, social or even political desiderata whose validity is not likely to be destroyed by the plan. The latter, however, usually does introduce new objectives and if policies are to be wisely chosen, this fact has to be squarely recognized. This entails some adjustment in priorities, and across those salients—well-defined and narrow, and in most cases not very numerous—on which the development plan requires action that will not otherwise be taken, other objectives may have to give way.

The violence done to these other objectives can be minimized by the avoidance of over-generous treatment of the entrepreneurs whose co-operation is being sought. In the provision of incentives, it is proper for the Government to be reluctant and cautious. This is another argument for adequate attention to the general business climate. The less the risk of sudden, frequent or arbitrary changes in official attitudes and policies the more responsive are the entrepreneurs likely to be, even to relatively small stimuli. Where uncertainties are great, by contrast, even extravagant inducements may not suffice to bring about the desired investment.

Incentive measures, moreover, need not be permanent and unconditional. Whatever the inducement—a mineral concession, preferred tax status or a protective customs duty—it is generally preferable to make it a limited and measurable one rather than open-ended and indefinite. While the arrangement should be meticulously honoured during its currency, its renewal should be subject to a performance test and a comprehensive review in which output and cost are appraised in the light of the immediately foreseeable needs of the developing economy.

No rule can be laid down regarding the duration of the privilege: the nature and magnitude both of the government sacrifice and of the investment it is intended to promote have to be taken into account.

While too long a period means an unnecessary abdication of the Government's freedom to use its economic tools, too short a period may either fail to exert the desired stimulus or introduce an undesirable element of uncertainty into the economy as well as an avoidable problem of administration. In general, experience indicates that the more comprehensive the incentive—that is, the more policy instruments involved—the sooner should its operation be reviewed for cost and consistency.

The need for internal consistency in the policy package is most obvious in the case of direct controls over access to a particular scarce resource. If a new investment is to be made, it is necessary to make appropriate allocations of all the required resources, even though the various rationing systems are conducted by different ministries applying different criteria. But in some cases, the denial of an allocation may also have implications for investment and production decisions and hence for the use of policy instruments. If foreign exchange is not made available for importing a particular good, for example, the implicit protection of the market may make its local production profitable. This will absorb other factors of production. If this conflicts seriously with plan needs, some disincentive—such as an excise tax or a higher profit tax—may be the logical corollary to the original system of controlling the available supply of foreign exchange.

Where, because of the scarcity of the resource, control over its use is instituted in order to give plan needs due priority, the most obvious collateral policy would involve measures to overcome the shortage. In most developing countries, such measures might include special encouragement of export activities to ease a foreign exchange stringency modification in price policy—such as the institution of official support levels or the raising of price ceilings in the case of the commodities the production of which was lagging—increased budgetary provision for research and training in the area of deficiency, and even arrangements for institutional and organizational experimentation such as reform of tenure or government participation in the sector in question. While the taking of positive collateral action may not always be feasible, there is a constant obligation on the part of the Government to make sure that it is not contributing to any impediment to plan fulfilment by the inconsistent use of some relevant economic instrument.

Accommodating short-term exigencies

It is proper for Governments to strive to reduce uncertainties, to create the sort of economic climate in which the energies and resources of the private sector are harnessed most naturally to the development intentions of the plan and to deploy a coherent and mutually reinforcing set of policies to guide the private sector where its spontaneous actions need directing, stimulating or damping. In the real world, however, a developing country is rarely in a position to pursue these goals single-mindedly. The structure of its economy—with its narrow industrial base, its shortages of skills and capital and its many physical and economic immobilities—is not such as to favour smooth and stable growth. And its dependence on imports for much of its plant and equipment and on an often limited range of primary commodities for most of its foreign exchange earnings makes it extremely vulnerable to the impact of external changes over which it has very little control.

When exogenous events threaten the internal or external balance of the economy, the policy instruments that have been deployed in directing the private sector towards the fulfilment of the plan intentions may have to be realigned. This contingency needs to be kept in mind whenever a policy package to induce desired action in the private sector is assembled. It suggests particular caution in the use of instruments that are likely to be required to counter any disequilibrating tendencies that may later emerge.

One such instrument is credit. It is awkward for a Government to find itself committed to making advances to particular segments of the economy at a time when the emergence of inflationary pressures has dictated a stringent monetary policy and restraints on credit. In many developing countries, the most vulnerable resource is foreign exchange and its over-liberal use to encourage the creation of new capacity can have similarly awkward consequences if for any reason external payments difficulties should later develop: the Government may find itself forced to cut down the allocation of foreign exchange for the importation of current inputs for established concerns while at the same time providing for the setting up of new facilities.

The gravity of such situations depends in part on the content of the plan. In general the greater the extent to which the plan is addressed to correcting the difficulties lying at the root of the imbalance the less will be the conflict between the economic measures that constitute the plan implementation strategy and those that are called for by the exigencies of actual current developments. A plan that aims at a rapid expansion in the output of an appropriate selection of goods will be less vulnerable to emergency action necessary in the face of a sudden increase in inflationary pressures than a plan whose main content is infrastructure and other forms of investment with long gestation periods. Similarly, a plan that focuses particularly on the export sector might not suffer unduly from the action that a balance of payments emergency might demand. In this, as in other cases, the time element is the critical one and the difficulty should not be underestimated. While export promotion or import substitution may be the least dangerous strategy for the plan of a country with a chronic external imbalance, every project so designed may involve immediate claims on foreign exchange and thus turn out to be vulnerable in a severe short-term balance of payments crisis.

In any conflict between short-term necessities and long-term objectives, it is the latter that inevitably have to yield. When a short-term "stabilization programme" is superimposed on a longer-term "development plan" (and there have been many such cases in recent years) the private sector tends to be reinforced in its all too common opportunistic attitudes. Speculation with existing assets becomes more profitable—and even less risky—than investment in new facilities. Credibility is reduced not only of the particular plan itself but also more generally in the Government's ability to carry through any longer-term plan.

While it may be impossible to avert short-term imbalances, steps can be taken to minimize their effects on longer-term development and on the attitude of the private sector towards the Government's efforts to plan such development. As indicated above, the plan itself may be directed towards remedying these weaknesses in the economy—food supply and exports, for example, both of which are overwhelmingly private sector activities in most developing countries—that are among the chief contributors to critical shortages or disequilibria.

The machinery established for the purpose of facilitating the necessary dialogue between the Government and at least the key elements in the private sector is put to a special test in periods of short-term emergency. Its efficiency is to be measured in part by its contribution to the process of smooth adjustment—deferment with the least disruption, plan modification with the least loss of confidence. In this it is likely to be assisted by a more flexible approach to longer-term planning and a greater emphasis on annual reviews and decisions regarding the course of action in the period immediately ahead. Governments, with varying degrees of intent, use their own budgets for this purpose; the problem they have to meet is to use the consultation machinery to carry part at least of this "rolling over" process into the private sector, thus avoiding sudden reversals in policy with their consequent damage to the credibility of the longer-term plan.

Whatever the success of the Government in inducing appropriate spontaneous responses in the private sector, it has to follow through with the necessary modifications in the way its own policy instruments are being deployed. In countries that are particularly exposed to significant fluctuations or prone to recurrent imbalances, the means for guiding the private sector to fulfil the designated plan targets should be selected with a view to their sustainability in the face of the most likely contingencies. In many developing countries, this means that particular care has to be exercised in the way in which claims on foreign currencies are allowed to build up through the growth of foreign-owned and import-dependent industries.

By deploying its economic weapons in the interest of stability, by avoiding arbitrary actions, by minimizing the number and extent of changes in policy and by deliberately setting out to reduce unnecessary uncertainty, the Government may be able to lower the rate at which, in most developing countries, private entrepreneurs tend to discount the future. In one important sense, planning is itself an exercise in extending the time horizon of the decision makers in the business community: the closer the entrepreneur can be brought to identifying the future of his own concern with that of the economy as a whole, the less leverage will have to be exerted in order to achieve compliance with plan objectives and the greater freedom the authorities will have in meeting short-term difficulties without disrupting longer-term programmes.

The international community may also help individual developing countries to correct temporary imbalances with minimum damage to soundly based growth. If additional resources can be provided while a country is making the necessary adjustment to its economic policies, the planned effort to expand production need not be as seriously interrupted as might otherwise be the case—to the great advantage of the efficiency of the private sector and of the planning process as a means of accelerating development in a market economy.

SUMMARY

In order to maximize and spread the benefits of a soundly based development plan, it is most desirable to involve the private sector—and especially the key productive elements—in the planning process. The need to do so increases with the proportion of total output produced in the private sector and with the comprehensiveness of the plan. The more closely the private sector identifies itself with the general objectives and specific targets of the plan, the better are the prospects for successful implementation.

In order to motivate the private sector effectively, the Government must convince it that not only is the plan consistent, feasible and desirable but also that it will be kept so by regular review, and that the official component will be carried out. In the case of a country launching its first development plan, especially where relations between the Government and private business have been less than satisfactory, special steps may have to be taken to improve the economic climate and ensure the co-operation of the private sector.

Other things being equal, it is generally easier to obtain the requisite degree of identification if the Government is able to arrange for the participation of the private sector in the formulation of the plan, especially if this embodies structural changes in the economy or production targets to be fulfilled in the private sector itself. The nature of the involvement depends to a large extent on the structure of the industry in question: the essential contacts that government requires are with the principal decision makers—in both management and labour—who determine production and investment policy.

Experience suggests that there are three degrees of involvement: (*a*) close and continuous in the case of strategic sectors in which a lag is likely or would be potentially disruptive or for which the plan intends structural or institutional changes, (*b*) systematic but less close for other production sectors and (*c*) general and motivational for the economy as a whole. Very few developing countries are administratively equipped to provide for the second of these; priority has to be given to the creation and operation of machinery through which the Government can ensure the co-operation of the key elements in the private economy.

Whatever the consultation machinery, it is essential to operate it at the appropriate substantive level, whether technical or economic. Thus the nature of the machinery is determined in part by the capacity of the civil service to work with it, and use it as occasion demands—for *ad hoc* negotiation, for technical consultation or for regular surveillance—along with the representatives of private industry.

Where a strategic segment of the private sector is not appropriately organized for consultation—as may often be the case in agriculture, for example—the Government may have to take special steps to keep it from acting as a drag on the rest of the economy. These may include the creation of new institutions for informing individual producers, for administering such incentives as may prove necessary and for assisting in the process of economic or technical reorganization in the interest of raising productivity.

In most developing countries, the strategic elements in the economy for which specific arrangements need to be made include the producers of selected goods vital for investment or consumption and of major export commodities and (where privately owned) transport and power. Unless these industries fulfil their targets, bottle-necks are likely to develop, and the whole plan may well be jeopardized. Agriculture, which provides not only local food-stuffs but also much of the foreign exchange earning capacity in most developing countries, is generally the most difficult element in the private sector to integrate into a development plan and needs special attention.

In relation to a normal plan period of five years, the time required to increase capacity in many of the strategic sectors is often rather long in most developing countries. Arrangements to expand needed facilities have therefore to be effected early in the plan, immediately after targets have been finalized, if imbalances are to be avoided. This re-emphasizes the importance of early involvement of the relevant key elements of the private sector in the planning process, of the credibility of government intentions and of an economic environment conducive to the extension of the time horizon for business decision-making.

If investment can thus be achieved through the normal decisions of businessmen acting in anticipation of increases in demand for the product, the necessity of using special incentives is minimized. This is desirable, because the instruments at the disposal of Governments for bringing the private sector into line with the plan are for the most part the ordinary means of economic management. These are the direct and indirect methods of guidance and control required for maintaining stability in the economy in the face of exogenous forces, and it is often awkward to use them simultaneously to promote a particular growth pattern.

The instruments available for influencing the private sector are relatively blunt in the circumstances of most developing countries. Because of the low degree of competition in much of the industrial sector as well as the ever-present danger of inflation characteristic of most developing countries, profit incentives tend to have less influence on investment and production decisions than they do in a more sensitive economy: to stimulate supply, it may be necessary to offer prospective gains large enough to be inimical to cost stability. Direct controls over scarce factors are usually more effective but experience shows them to be better at inhibiting than at stimulating. Moreover, administrative machinery is often too weak to allow successful discrimination in accordance with need—in the provision of credit, for example, in running a dual price system to shield consumers of a commodity from a higher price paid to encourage producers, or in the allocation of foreign exchange in order to boost a lagging sector and remove a supply bottle-neck.

In many developing countries, most of the economic control policies are actually in operation at any one time. This adds to the problem of putting together a combination of measures which can be deployed in a discriminatory fashion to encourage the specific private sector development that the plan requires. The constituent elements of the policy package need to be consistent with one another and to represent, as far as possible, the least-cost combination, that is, the combination likely to do the minimum of violence to other objectives, such as increasing government revenue, saving foreign exchange or restraining domestic costs.

In selecting the instruments with which to guide the private sector, the Government has also to keep in mind the measures that may prove necessary to maintain economic stability in the face of pressures that may arise exogenously during the plan period. Where foreign exchange is a particularly scarce resource, for example, it is hazardous for a Government to impair its ability to take restrictive action by making undue commitments, even tacitly, in respect of future allocations in order to induce particular private sector investment.

Even after the most appropriate combination has been selected, the effective use of such instruments —for the purpose of keeping the private sector in line with plan requirements and facilitating such modifications in plan targets and phasing as become necessary—depends on the smooth and timely operation of current reporting and evaluation machinery, something that itself has proved difficult to attain in most developing countries.

The certainty of appropriate action on the part of the private sector, whether spontaneous or induced, depends very largely on the confidence generated by the whole environment—political, institutional and social as well as economic. The functioning of the capital market, of the tax system and of labour and mercantile laws, as well as all the other elements of "climate", will affect business decisions and influence the response of workers and investors both to the prospects of expansion in demand and to the offer of special incentives. Even effective methods of consultation and a wise choice of inducements may be insufficient to offset serious deficiencies in economic environment. In this context, the effect of the plan on the distribution of incomes is likely to have an important bearing on the way in which the private sector collaborates in the implementation of production plans.

Because of the vulnerability of most developing countries to exogenous forces, the international community can make a major contribution to the implementation of development plans by maintaining the demand for the export products of the countries concerned. And if in its effort to accelerate its rate of growth a developing economy does get out of balance, the international community can provide resources to help restore the balance with the least disruption of the plan the country in question is trying to implement.

Chapter IV

RECENT EXPERIENCE IN THE IMPLEMENTATION OF DEVELOPMENT PLANS

INTRODUCTION

The preceding chapters have examined some of the problems and experience of developing countries in devising more effective instruments for the implementation of plans. The present chapter presents a brief review of recent economic trends in a number of countries which have endeavoured to use their plans consistently as guidelines for development policies. The analysis has necessarily been confined to countries for which data covering several years of their planning periods are available. For several of these countries, the data permit review of the whole of the period spanned by recent plans; for others, the data refer to shorter periods; but in no case is the period less than three years. In view of the small number of countries reviewed any generalization regarding progress in plan implementation based on the experience described in this chapter would be hazardous.

It must be emphasized that even a plan period of four or five years is often too short for an appraisal of the effectiveness of long-term development policies; the full influence of such policies may become evident only over a longer period. Further, within the relatively short period covered in the present review, the effects of public policies on growth may be offset by developments which are beyond the control of the policy makers. The attainment or non-attainment of the physical targets of a medium-term plan is thus not necessarily an indication of the effectiveness of plan implementation. An attempt to determine the contribution of policy measures to quantitative changes in output and expenditure would go beyond the scope of this review, and the present chapter therefore confines itself to comparisons of quantitative achievements with plan targets and to a brief examination of some of the policies which Governments have pursued in order to realize targets.

Recent trends in output and investment

In most of the countries reviewed in the present chapter, performance during the plan period has been quite encouraging even though a number of countries have not attained the over-all growth rates envisaged in their plans. Ten of the twelve countries included in table 7 have achieved higher rates of growth for gross domestic product than they had recorded in the five years preceding their recent plans. Of these ten countries, China (Taiwan), Malaysia, Pakistan, Republic of Korea, Sudan and Uganda have also exceeded their planned growth rates, while the United Arab Republic has come close to attaining its targets. The performance of most of the countries, in fact, compares favourably with the average rate of growth of slightly more than 4 per cent *per annum* recorded by the developing regions as a whole during the first half of the 1960's; and in several instances, it exceeds the target rate of 5 per cent *per annum* established under the United Nations Development Decade.

Almost all countries have increased the share of investment in the gross domestic product and a number have virtually attained or even exceeded the rates of increase in gross investment which their plans had envisaged (see table 8). However, experience has again demonstrated the difficulty of making accurate estimates of the investment required for the attainment of a projected rate of increase in output. In the United Arab Republic and Venezuela, for instance, investment has increased as fast as, or faster than, planned while the over-all growth rate has fallen short of the target. To some extent, such disparities can be explained by the influence of the agricultural performance on the growth of the economy as a whole. In agriculture, the relationship between new investment and increases in output tends to be particularly uncertain, the more so over relatively short periods when trends in output are obscured by the influence of weather conditions.

Success in achieving the planned rates of growth in total output has, in fact, depended in large measure on the performance of agriculture. Of the countries which have exceeded their planned growth target for gross domestic product, only the Republic of Korea has experienced a shortfall in agricultural production. Conversely, among those which have failed to attain their over-all growth targets, only the Sudan has met its target for agriculture. Very much the same holds true of industrial growth. Those

Table 7. Planned and actual annual rates of growth in gross domestic product[a]

(Percentage)

Country	Planned[b]	Actual in pre-plan years[c]	Actual in plan years 1960	1961	1962	1963	1964	1965	Average
China (Taiwan)	8	6.7		8.2	8.0	11.3	14.2		10.4
Venezuela	8	7.5				4.1	8.0	5.1	5.7
United Arab Republic	7	5.0	6.1	2.6	8.7	8.7	6.6		6.5
Morocco	6	—0.4	3.9	—3.2	12.8	5.0	0.9	2.3	3.6
Philippines	6	5.2			3.5	5.3	4.1	5.4	4.6
Republic of Korea	6	4.9			4.1	9.3	8.9	8.1	7.6
Tunisia	6	1.6			1.7	3.7	6.7	6.1	4.6
India	5.5	3.6		2.6	1.9	5.0	7.7	(—4.2)	4.3[d]
Sudan	5	3.2		12.4	1.0	5.8	2.9	...	5.5
Pakistan	4.5	2.5	5.1	5.7	4.0	8.2	4.3		5.5
Malaysia[e]	4	3.5		6.1	5.1	7.5	5.4	7.3	6.3
Uganda	3.5	3.2		—2.0	0.7	9.7	5.8	4.8	3.8

Source: United Nations, National Accounts questionnaire, 1966, *Yearbook of National Accounts Statistics, 1965* (Sales No.: 66.XVII.2), national development plans, and national sources.

[a] For Malaysia, Pakistan and Uganda, gross domestic product at factor cost; for China (Taiwan), Philippines and the Republic of Korea, gross national product at market prices; for United Arab Republic, gross national product at factor cost; for India, national income; for the remaining countries gross domestic product at market prices.

[b] Data refer to the plan periods as a whole which were as follows: China ((Taiwan), 1960-1964; Venezuela, 1963-1966; United Arab Republic, 1960/61-1964/65; Morocco, 1960-1964; Philippines, 1962/63-1966/67; Republic of Korea, 1962-1966; Tunisia, 1962-1971; India, 1961/62-1965/66; Sudan, 1961/62-1970/71; Pakistan, 1960/61-1964/65; Uganda, 1961/62-1965/66.

[c] Data for pre-plan years refer to the period between 1953-1954 and 1959-1960 or a shorter period where data for years stated are not available; they have been conformed as far as possible to plan definitions.

[d] Average for 1961-1964; this may be taken as more representative of the trend than the average growth rate for 1961-1965 in view of the fact that the reduction in the national income in 1965 was the consequence of a severe drought.

[e] Former Federation of Malaya only.

Table 8. Gross investment: Annual rate of increase and share in gross domestic product

(Percentage)

Country	Annual rate of increase in investment[a]: Planned	Actual[b]	Share of investment in gross domestic product, Actual share[c]: Base year	Latest year
Morocco	21	8.5	10	13
Pakistan	20.5	18.1	10	18
Republic of Korea	15.5	15.7	11	14
Philippines	12	4.6	11	11
Malaysia	11.5	11.6	14	19
United Arab Republic	11.5	11.4[d]	12	18
India	10	7.5	11	14
Tunisia	9.5	12.3	19	25
Venezuela	8.5[e]	13.1	14	17
China (Taiwan)	7	11.2	18	19
Sudan	5	11.5	12	18
Uganda	...	9.5	12	16

Source: See table 7.

[a] Plan data for the Sudan refer to gross fixed capital formation; for India, net investment; for other countries, total gross investment. Actual data for Morocco, Republic of Korea, Sudan, Tunisia, Uganda and Venezuela refer to gross fixed capital formation; for other countries, total gross investment.

[b] Data refers to years shown in table 7.

[c] The term "base year" refers to the year preceding the first plan year; "latest year" is the terminal year of the plan or the latest year for which data are available as indicated in table 7.

[d] Estimate of the Secretariat.

[e] Rate of increase from 1960 to mid-point of plan.

countries which have attained or surpassed their targets for the rate of growth in total output have fulfilled or exceeded their expectations with regard to the expansion of industrial output.

Another factor which has significantly influenced the pace of development during the plan period has been the performance of exports. World demand for primary products has been relatively buoyant since the early 1960's and the countries reviewed in this chapter have benefited in varying degree from this trend. As discussed more fully below, several countries have exceeded the projected growth rate for exports, sometimes by a very substantial margin. Thus, the unexpectedly vigorous expansion of exports in China (Taiwan), Malaysia, Pakistan and the Republic of Korea has greatly facilitated the execution of development projects and the attainment of the projected growth of the gross domestic product. On the other hand, in some countries, shortfalls in the domestic production of food-stuffs and essential materials and consequent inflationary pressures have necessitated increases in non-developmental imports which have absorbed unforeseen gains in export receipts. It is evident that, among the countries which have fulfilled or exceeded their plans for total output, the performance of agriculture, industry and exports has also usually been better than expected. Expansion in each of these sectors has no doubt tended to support, and reinforce, expansion in the others. But it is not to be concluded that there has been any simple causal relationship at work. A strong rate of increase in exports, for example, has not been sufficient in itself to enable countries to achieve their over-all growth targets though it has contributed significantly towards accelerating the pace of development in countries where other factors have favoured relatively rapid growth. It will become clear from the discussion which follows that the forces accounting for good or poor over-all performance have invariably been complex and that, in every country, progress in plan implementation has varied considerably from sector to sector.

PERFORMANCE IN AGRICULTURE

In recent years Governments in developing countries have become more acutely aware of the importance of agriculture in the development process. While economic development had been considered for many years to be virtually synonymous with industrialization, progress in agriculture is nowadays recognized as essential for development. Many of the development plans of the 1960's have accordingly given increased attention to agriculture; and recent plans have therefore set growth targets for agriculture which were generally well above the growth rates achieved in the years preceding the plans (see table 9).

Table 9. Planned and actual rates of growth in agricultural production

(Percentage)

Country	*Planned*	*Actual*[a] *Plan years*	*Actual*[a] *Pre-plan years*
Venezuela	8	6.6	5.1
China (Taiwan)	5.5	6.4	3.8
Morocco	5.5	2.6	—0.7
Republic of Korea	5.0	3.7	2.9
United Arab Republic	5.0	3.3	3.1
India	4.5	2.5	2.2
Sudan	4.0	5.3	3.0
Tunisia	4.0	2.7	3.3
Malaysia	3.0	4.0	2.9
Philippines	3.0	2.6	1.1
Pakistan	2.5	3.3	0.6

Source: See table 7.

[a] Plan years refer to those shown in table 7. For pre-plan years, see foot-note *c* to table 7. Actual growth rates are based on data relating to value added in constant prices, as defined in national accounts.

The renewed interest in agricultural development has not arisen solely, or even primarily, from a general desire to raise productivity and income in a lagging sector of the economy. It was the evidence of a growing imbalance between food production and food requirements and, in some cases, between industrial capacity and the domestic production of agricultural materials for industry, which has forced Governments to take a fresh look at their problem of agricultural development. Further, in the face of unfavourable long-term trends in world demand for some of the major export products of developing countries, export diversification has also become a matter of increasing urgency, demanding early action to expand output of agricultural products with more favourable export prospects.

The need to increase the production of staple food-stuffs for the domestic market has been most urgent in food-deficit countries, such as India, Morocco, Pakistan, Sudan and United Arab Republic, most of which have come to depend increasingly on food aid shipments under United States PL 480 to cover shortfalls in domestic output. Their growth targets for agriculture as a whole have therefore been determined in large measure by the objective of eliminating the food deficit as rapidly as possible, and, in particular, the shortfall in the domestic production of food-grains. As table 10 shows, almost all the food-deficit countries have envisaged a substantial acceleration in the growth of cereal production. Among cereals, rice has been given emphasis, notably in Pakistan and the United Arab Republic, in view of its export potential as well as its role as a staple

Table 10. Planned and actual annual rates of increase in food-grain production in food-deficit countries

(Percentage)

Country	Total			Per capita		
	Planned	Actual		Planned	Actual	
		Plan years[a]	Pre-plan years[b]		Plan years[a]	Pre-plan years[b]
Venezuela	12.0	5.9	10.2	8.5	2.4	6.2
Sudan	8.5	7.4	2.3	5.5	4.4	—0.8
United Arab Republic	6.0	4.0	...	3.5	1.0	...
India	5.5	2.4	3.6	3.5	—	0.5
Philippines	5.5	1.9	3.6	2.1	—1.3	0.3
Pakistan	4.0	6.0	2.3	2.0	3.8	0.2
Morocco	2.5	1.7	—3.7	0.5	—1.0	—6.3

Source: Based on Food and Agriculture Organization of the United Nations, *World Crop Statistics* (Rome, 1966) and national development plans.

[a] Years covered are from beginning of plans as indicated in table 7 to 1964 or 1964/65.

[b] Data generally refer to the period 1953-1954 to 1959-1960 or a shorter period where data for the years stated are not available.

in the national diet. At the same time, several countries, including India, Pakistan and United Arab Republic, have aimed at expanding production for the domestic market of commercial food crops, such as sugar cane, and of cotton, hides and skins, oil-bearing crops, tobacco and other materials for their growing industries. Fruit, vegetables, sugar, spices, palm products, coarse grains and textile fibres have been among the agricultural commodities on which plans had variously focused in the context of programmes for export diversification.

During the plan years covered in the present survey, most countries have succeeded in accelerating the growth of agricultural production. But only about one third of the countries have attained or exceeded the planned growth rate; these latter include China (Taiwan), Malaysia, Pakistan and Sudan (see table 9). Among the major food-deficit countries, only Pakistan, Sudan and Venezuela have achieved sufficiently large increases in cereal production to reduce their dependence on imports. *Per capita* production in the United Arab Republic appears to have been insufficient to meet rising consumption requirements, most especially those of the low-income groups which have benefited from the Government's wage policy. In Morocco and the Philippines, *per capita* production of food-grains has declined. In India, the level obtaining in 1961/62 was barely maintained up to 1964, and with the disastrous crop failure of 1965 it thereafter fell to well below the pre-plan level.

Broad production indices for agriculture which relate to relatively short periods of from three to five years, such as those covered in tables 9 and 10, are only of limited value as indicators of either the effectiveness of policies for the achievement of plan objectives or of trends in output. Some important measures for agricultural development are of a long-term character and their effect on output may not become apparent within a single plan period. Furthermore, within a relatively short time span, the vagaries of the weather may offset or exaggerate the effect of measures to accelerate the growth of output, resulting in significant deviations from production trends.

Data on the fulfilment of investment targets for agriculture are potentially better indicators of the effort devoted to agricultural development than are production indices, but these, too, have their limitations. For one thing, much of the investment which contributes to agricultural growth takes place outside the sector. Major multipurpose irrigation schemes such as the Aswan Dam project in the United Arab Republic, rural electrification schemes, or the establishment of factories producing agricultural inputs such as fertilizers, contribute no less to agricultural development than does investment in the agricultural sector itself. Furthermore, a substantial proportion of developmental expenditure in agriculture is not investment in the technical sense and is not recorded as such. Data on agricultural investment therefore reflect only one part of the effort to attain agricultural growth targets.

The share of total gross investment which was to be devoted to agriculture according to the plans ranged from 9-10 per cent in the Philippines and Venezuela to 39 per cent in Tunisia (see table 11). China (Taiwan), the Sudan and Venezuela have actually allocated a larger proportion of total investment to agriculture than they had planned. In Pakistan and the United Arab Republic, the allocation of resources for investment in agriculture has come close to the proportion envisaged in the plans; but in Pakistan the growth of total investment in real

Table 11. Planned and actual share of agriculture in total gross investment

(Percentage)

Country	Share of agriculture in total investment		Average rate of growth of total investment	
	Planned	Actual[a]	Planned	Actual[a]
Tunisia	39	21	9.5	12.3
Sudan	25	26	5.0	11.5
United Arab Republic	20	17	11.5	11.4
China (Taiwan)	17	18	7.0	11.2
Republic of Korea	17	9	15.5	15.7
India:				
Total	16	...	10.0	7.5
Public	14	13	...	...
Pakistan	15	13	20.5	18.1
Venezuela	10	13	8.5	13.1
Philippines	9	6	12.0	4.6

Source: See table 7.
[a] Years covered are those shown in table 7.

terms has fallen short of the target and the amount of real resources devoted to agricultural investment has consequently also failed to come up to the planned level.

Failure to fulfil investment plans has not necessarily been a consequence of inadequate plan implementation. In some cases, the emphasis in programmes for agricultural development has been shifted from more capital-intensive projects to projects involving smaller capital outlays as well as to general developmental expenditure deemed to be of greater importance for the achievement of the plan objectives. This has been the case, for instance, in India. However, in many cases the non-fulfilment of investment targets has been due to a failure to meet the policy requirements of plans for the agricultural sector and to difficulties encountered in the execution of investment projects.

Measures for agricultural development

In developing countries, the implementation of policies designed to stimulate the growth of agricultural output is frequently impeded by institutional deficiencies and by ignorance and resistance to change on the part of the large numbers of producers who constitute the agricultural sector. The task of many Governments seeking to overcome agricultural stagnation and backwardness is therefore not merely one of undertaking and stimulating investment, providing incentives for production and ensuring an adequate supply of the necessary inputs; it also embraces broader and more complex problems of changing the institutional framework so as to permit the other measures to be used more effectively. The corner-stones of agricultural development policy in developing countries have thus been measures of four kinds: public investment in infrastructure projects, measures to encourage the adoption of improved cultivation methods, the provision of production incentives, and measures to reform the institutional framework of agriculture.

The effective implementation of programmes for agriculture has usually involved some combination of these measures. The weight given to any one in the "policy package" has varied according to the nature of the major obstacles to growth, the structure of the economy, its resource endowment, the financial and manpower resources available to the Government, the attitudes towards institutional reform, and the prevailing views about the role of the State in economic life. It has been relatively easy for Governments to get domestic support and external financial assistance for major public investment projects and these have generally been accorded high priority in agricultural programmes. Measures to bring about improvements in production methods have also been widely employed, but their effectiveness has been limited by institutional factors and the farmers' resistance to change on the one hand, and by shortages of qualified personnel for their administration on the other hand. Institutional reforms, though widely recognized to be essential for progress in agriculture, have frequently proved to be the most difficult to implement. And failure to carry out reforms has been a common cause of inadequate progress in the implementation of programmes for agricultural development. The importance of reforms arises not only from the fact that antiquated land ownership and tenure systems and other institutional deficiencies have a direct bearing on productivity in agriculture but also because these systems diminish the effectiveness of other instruments of agricultural policy, such as production incentives, agricultural extension work and the introduction of new techniques. It is perhaps no exaggeration to say that in many countries the failure of Governments to put the necessary reforms into effect has been largely responsible for the disappointing results of efforts to accelerate the growth of agricultural output.

Public investment in agriculture

Major areas of public agricultural investment have been irrigation, land clearance and drainage schemes designed to enlarge the area under cultivation and to increase the productivity of the cultivated land. While the capital cost of such schemes is high, they contribute to agricultural development both by creating permanent additions to productive capacity and by facilitating the introduction of new production methods.

In the period covered by recent development plans, the opening up of new land for cultivation has contributed significantly to the growth of agricultural production in several countries. In Uganda, for instance, the cultivated area was apparently increased by 30 per cent in the years from 1961 to 1964; in the Republic of Korea it was increased by 11 per cent, in Malaysia by 8 per cent and in Pakistan by 3 per cent. In China (Taiwan) and the United Arab Republic, the area under cultivation has not increased significantly in the plan years covered in this review, but in the United Arab Republic large new areas are due to come into production in the late 1960's when irrigation schemes connected with the Aswan High Dam will be completed. In the Sudan, as in the United Arab Republic, heavy reliance has been placed on the expansion of arable land through a number of irrigation schemes deriving from the Nile waters, and the area under cereal crops and cotton was estimated to have increased from 1960 to 1964 by over 40 per cent. Substantial increases in the acreage devoted to cereals have also occurred in Ecuador and Venezuela where virgin land is plentiful.

Large-scale irrigation and land development projects have played a major role in the development programmes of Malaysia, the Sudan and the United Arab Republic. But a number of countries have given increased attention in their recent plans to smaller projects designed to improve the water supply on cultivated land and to yield quick benefits at lower cost by using existing capital more effectively. In many cases, the completion of major projects had not been followed up with the construction of the necessary facilities to take full advantage of the additional water potential which had been created. In India, for instance, lags in the construction of field channels and reservoirs have been mentioned as a factor in the relatively slow progress of agriculture under the third plan. During the implementation of the plan there was, in fact, some shift in emphasis from major to minor irrigation works and the Government has proposed to give increased attention to the latter in its fourth plan. Pakistan initiated under its second plan a highly successful programme for ground water development to supplement the available water resources on irrigated land. During the plan period, some 30,000 tube wells were installed by farmers with government assistance and by the Government itself, which improved irrigation over an area of some 4 million acres. The success of the programme has been related, in large measures, to its co-ordination with a rural electrification programme which has made the operation of the tube wells possible. It has been estimated that ground water development in West Pakistan contributed as much as one third to the increase in crop production of that region during the period 1960/61 to 1964/65.[1]

Measures to increase yields

Programmes for increasing yields on existing farms have formed part of all development plans but their implementation has raised a host of problems. In order to raise agricultural productivity through improved inputs and methods, it is usually necessary first to persuade the farmers to use them and then to ensure that they are correctly and effectively employed. The procurement and distribution of inputs such as chemical fertilizers, pesticides and improved seed varieties are themselves difficult operations since developing countries usually lack adequate transportation and distribution channels and are deficient in domestic capacity for the production of these inputs. But the more intractable problem is that of the persuasion, training and guidance of the—frequently reluctant—prospective users. Its solution requires considerable numbers of qualified extension workers who are not only familiar with the techniques they have to teach but are also skilful organizers and educators.

Yields per acre are strongly affected by climatic factors, and changes over a relatively short period do not necessarily reflect trends in agricultural productivity. But a comparison of average yields per acre recorded by countries during recent plan years with those of the preceding five-year period shows a fairly consistent tendency towards an increase in yields for the major cereal crops (see table 12). Apart from the Sudan, yields have generally increased in rice production and, in most cases, the same holds true of wheat and other cereals as well.

Relatively large improvements in rice yields have been achieved in Pakistan, Malaysia and Venezuela, in maize yields in the United Arab Republic, and in wheat and barley yields in Tunisia; in these coun-

[1] Government of Pakistan, *Third Five-Year Plan (1965-70)*, p. 396.

Table 12. Major cereals: Yields per acre and changes in area sown

Country and commodity	Area yield: Pre-plan years[a] (Hundreds of kilogrammes per acre)	Area yield: Plan years[b] (Hundreds of kilogrammes per acre)	Change in area sown[c] (percentage)
China (Taiwan)			
Rice	12.3	13.8	—1.6
India			
Wheat	3.0	3.3	6.1
Rice	5.6	6.1	9.2
Millet and sorghum	1.8	1.9	2.2
Malaysia			
Rice	8.8	10.1	1.3
Morocco			
Wheat	2.5	2.7	—8.3
Rice	2.6	2.8	—7.0
Pakistan			
Wheat	3.1	3.3	9.7
Rice	5.6	6.6	14.9
Republic of Korea			
Wheat	4.8	3.7	13.5
Rice	11.9	12.6	7.2
Sudan			
Millet	2.7	2.6	45.0
Sorghum	4.1	3.8	14.6
Tunisia			
Wheat	1.4	2.0	—7.1
Barley	1.0	1.5	—5.8
United Arab Republic			
Wheat	9.4	10.5	—13.8
Rice	21.2	21.4	47.0
Maize	8.4	10.0	—10.2
Venezuela			
Maize	4.6	4.2	19.9
Rice	6.1	7.3	118.4

Source: Food and Agriculture Organization of the United Nations, *World Crop Statistics* (Rome, 1966).

[a] Average for five years preceding plan period.

[b] Years covered are from beginning of plan as indicated in table 7 to 1964 or 1964/65.

[c] From base year of plan to 1964.

tries, the improvements in yields of these crops have varied from at least 15 per cent to as much as 50 per cent. But in most countries, increases in yields of the major cereals have been within the range of 6-12 per cent. Although differences among countries in soil and climatic conditions variously affect the scope for increasing the yield of any particular crop, the wide variations in the increases which have been achieved suggest that, with improved inputs and irrigation, more could be achieved in a number of countries than has been the case in the past.

While important advances have been made in agricultural technology in the past decade, they have thus far had only a limited impact on agriculture in developing countries. Of the improved agricultural inputs which have become available, chemical fertilizers have gained wide acceptance and their increased use has contributed substantially to the advances in productivity which have been achieved. As table 13 shows, the consumption of chemical fertilizers has more than trebled during the plan period in Pakistan, has more than doubled in India, and has increased by 50 or more per cent in the United Arab Republic. Since a substantial proportion of the fertilizer used in developing countries has had to be imported, these increases in fertilizer consumption have been costly in terms of foreign exchange outlays; and they have often also involved large government expenditures in subsidizing the prices charged to users.

A number of countries have embarked on programmes for the establishment and expansion of domestic capacity for the manufacture of fertilizers. Pakistan, for instance, included in its second plan a programme for increasing fertilizer production to

Table 13. Consumption of fertilizers

(Thousands of tons of N, P_2O_5, K_2O)

Country	Nitrogenous fertilizers	Phosphate	Potash
China (Taiwan)			
Pre-plan average	102	34	28
1964/65	137	37	35
India			
Pre-plan average	210	40	21
1964/65	510	148	63
Malaysia			
Pre-plan average[a]	18	5	7
1964	31	4	14
Morocco			
Pre-plan average	6	16	5
1964	15	20	8
Pakistan			
Pre-plan average	22	2	...
1964/65	83	9	2
Republic of Korea			
Pre-plan average	181	67	8
1964	173	146	41
Sudan			
Pre-plan average	16	...	...
1964/65	23	...	...
United Arab Republic			
Pre-plan average	136	25	1
1964	198	44	2

Source: Food and Agriculture Organization of the United Nations, *Fertilizers—An Annual Review, 1965*.

Note: Pre-plan average refers to five years preceding plan period.

[a] Average of four years.

300,000 tons. The fact that the target was exceeded enabled the Government to step up the use of fertilizer without incurring additional foreign exchange expenditures. India had set a target for fertilizer production of 800,000 tons by the end of its third plan, but the capacity in operation by 1965 was only of the order of 600,000 tons. The unsatisfactory progress was attributed to difficulties in the implementation of private sector schemes. As a consequence of the shortfall in the planned expansion of domestic fertilizer production, outlays on fertilizer imports trebled from the first to the last year of the third plan. The United Arab Republic has apparently achieved the planned expansion in fertilizer production, but imports none the less increased substantially during the plan period. China (Taiwan) not only became self-sufficient in some of the major chemical fertilizers before the end of the plan period but it also began to export significant quantities.

In view of the increases in fertilizer consumption, improvements in yields appear to have been surprisingly small in many cases. One of the reasons for the limited achievements in this regard has been a failure to combine fertilizer use with other essential inputs, such as adequate irrigation. In India, for instance, the practice of spreading irrigation water thin in order to benefit the widest possible area has proved to be unsuitable for a more intensive cultivation based on increased use of chemical fertilizers. In many cases, it has also been found that the plant varieties commonly grown did not respond adequately to new cultivation techniques. In Pakistan, for instance, the use of fertilizer and intensified irrigation damaged crops of long-stemmed wheat; these have been subsequently replaced on an experimental basis by improved varieties, and excellent results have been obtained.

Price policy

The use of price incentives to stimulate agricultural production is being increasingly advocated. To some extent, this represents a reaction to the past tendency of Governments in many developing countries to focus, perhaps excessively, on the needs of industry and of urban-industrial populations in their price policies. This was true of development policy in the 1950's; and even in some of the recent plans, price policy has continued to favour the industrial sector, or has at least not been deliberately used as a means of stimulating agricultural production. But if price policy has not been more widely used despite recognition of its potential value as a means of stimulating production, the main reason lies in the difficulties encountered in implementation.

An important obstacle to the use of price incentives is the difficulty of making them effective in the traditional institutional environment of agriculture. Price measures often conflict directly with traditional patterns of marketing and credit, and they may encounter open opposition from those engaged in such activities. Unless a Government is able to ensure that prices designed to stimulate output do in fact benefit the producers rather than the merchants and middlemen, the over-all effect of price policy on production may be negligible and higher prices charged to the consumer or the subsidies paid by the taxpayer may go only to enlarge trading profits. But the effective enforcement of a price policy requires a competent field staff and the establishment of collection points where supplies can be marketed at the controlled price; and this presents considerable organizational problems.

Notwithstanding these difficulties, a number of countries have introduced minimum price support schemes for products destined for the domestic market as part of their recent programmes for agricultural development. The object of the price support schemes has been to eliminate excessive seasonal price fluctuations and to protect farmers against sudden price declines.

Pakistan, after dismantling various price controls in 1961, established minimum prices for voluntary sales of wheat and rice to the Government. At the same time, it built up buffer stocks to regulate the flow of supplies to the market. India began to relax restrictions in 1960 and to build up buffer stocks, but the accumulation of stocks had to be discontinued under the impact of the harvest failure of 1963/64. More recently, the Planning Commission has noted that

> "a . . . factor which contributed to slow growth in agricultural production was the absence of an effective price policy. Price support policy in the past was aimed at eliminating distress. But this did not provide the incentive needed for dynamic agricultural growth. Accordingly, in 1964, minimum support prices on a more realistic basis were fixed for rice and wheat in certain states . . . . Price and marketing policies will assume added significance during the Fourth Plan in the context of a massive effort for securing rapid increases in production".[2]

In several other countries the effects of inadequate price policies became apparent in the course of the implementation of plans, and efforts were made, often belatedly, to remedy the situation. In the United Arab Republic, for instance, the controlled price for rice is reported to have become increasingly inadequate—in the face of rising farm wages and other production costs—to secure the projected expansion of rice cultivation. But it was not until 1966, when the entire price structure was revised, that the Government proceeded to raise the con-

[2] Government of India, Planning Commission, *Fourth Five-Year Plan—A Draft Outline*, p. 174.

trolled price of rice sufficiently to furnish an incentive to an expansion of rice acreage.

Institutional reforms

It is widely recognized that the traditional system of land ownership and tenure is a major impediment to agricultural development in many countries. Although its reform has long been advocated on political, social and economic grounds, comparatively few countries have carried out far-reaching programmes.

In several of the countries reviewed in this chapter, land reform legislation had been enacted in the 1950's, or earlier, and its implementation had been completed before the formulation of their recent development plans. This was notably the case in China (Taiwan), Republic of Korea, Sudan and United Arab Republic. In other countries, including India and Pakistan, the implementation of earlier land reform legislation proceeded slowly and its completion was one of the objectives of current plans for the agricultural sector. In Ecuador and Venezuela, current plans for agriculture dealt extensively with various aspects of the implementation of the land reform programme.

The main features of land reform in most developing countries have been measures to improve the legal and economic status of tenants, the establishment of limits to the amount of land which an individual may own and the distribution of the "excess" acreage to landless peasants. In some cases, legislation has also provided for the consolidation of scattered holdings into viable units. In addition, a number of Governments have undertaken programmes for the distribution and settlement of State-owned land.

Tenancy reform has been designed to give tenants greater security of tenure and to replace share-cropping and similar practices by fixed cash rentals. Such reforms, apart from their stabilizing effect on rural society, were expected to yield economic benefits by encouraging tenants to invest in land improvement. Their implementation has generally encountered less opposition from landowners than other land reform legislation, and since these reforms have involved no large outlays of public funds, they have generally been given high priority. In China (Taiwan), India, Pakistan, United Arab Republic, and some other countries, reforms of the tenancy system had been virtually completed by the time recent plans went into operation, although formal changes have not necessarily eliminated all abuses associated with the old system.

Programmes for the consolidation of holdings, designed to make production more efficient and economical, have been undertaken in a number of countries under their recent plans. In India, for instance, the target set in the third five-year plan for the consolidation of 31 million acres appears to have been virtually attained by the end of the plan period. In Pakistan, where a similar programme was initiated, 7.8 million acres were consolidated in West Pakistan during the second plan. In East Pakistan, however, the consolidation of 90,000 acres undertaken at the same time was cancelled after 1962 when a commission of enquiry recommended against all involuntary consolidation measures.

The enforcement of acreage ceilings and the redistribution of land in excess of these ceilings have tended to be the weakest link in the implementation of land reform programmes. For one thing, these have been frequently opposed by politically powerful groups, and amendments to the legislation proposed by the Government have often limited their impact. This has been notably the case in countries such as India and Pakistan where land reform legislation is within the jurisdiction of state or provincial legislatures. In East Pakistan, for instance, an amendment introduced in 1961 to the land reform law of 1950 raised the acreage ceiling originally stipulated, and some of the land which had already been acquired by the Government was restored to its previous owners. In West Pakistan, about 2.2 million acres were acquired by the Government, but only one third had been distributed to tenants by the end of the second plan. The implementation of acreage limitation and of associated measures of land redistribution has also been delayed by the absence of cadastral surveys in many countries and by the lack of public funds for compensation payments and for investment in the construction of basic facilities required for new settlements. Financial stringency is said to have been one of the factors which have delayed the establishment of acreage ceilings and land acquisition in Ecuador, for instance. Shortage of qualified personnel to organize and supervise the development of the new farms has also been a bottle-neck in the implementation of land reform. Partly in order to forestall the emergence of these difficulties, some Governments have proceeded by stages, carrying out land redistribution at each stage in certain designated areas only. This has been done, for instance, in the Philippines under the land reform law of 1962, though even implementation on the limited scale envisaged in the law did not begin until 1964.

In China (Taiwan) and the United Arab Republic, where land reform had been completed before recent plans went into operation, some additional measures of land distribution have been carried out in the recent past. The Government of China (Taiwan) introduced in the late 1950's a system of land purchase grants and loans to enable tenant farmers to purchase the land they worked. Under this programme, acreage equivalent to 4 per cent of the cultivated land was acquired between 1960 and 1963, bringing the total amount of land redistributed since the inception of the land reform programme to 20 per cent of the acreage under cultivation. A special feature of the recent scheme has been the payment of a proportion of the compensation to owners in the form of stock in enterprises formerly owned by the Government. This was designed to serve as an inducement for landowners to part with this land and to engage in business activities. In the United Arab Republic, further limitations on landownership introduced in 1961 were expected to result in the redistribution of the ownership of an additional 6 to 7 per cent of the cultivated area.

Land reform by itself does not eliminate agricultural stagnation, and even in the long run its effect on growth depends, among other things, on whether or not the new holdings are of an appropriate size for the economic cultivation of the crops to be grown on them. This has not always been the case. Faced with this problem, some Governments, such as those of China (Taiwan), Pakistan and the United Arab Republic, have encouraged the establishment of producer co-operatives. But the shortage of qualified managers and the reluctance of farmers to participate in such projects have limited the scope for action along these lines. The success of land redistribution also depends to an important extent on its effective co-ordination with a variety of other measures. These include the establishment by the Government of infrastructure facilities, such as roads, irrigation and storage, and the provision of credit, marketing services, technical advice and educational and training facilities. The implementation of such a programme requires substantial financial resources and an adequate staff of competent administrators and technicians, neither of which is readily available in most developing countries.

But in the few cases where a co-ordinated programme has been put into effect, highly satisfactory results have been achieved. In China (Taiwan), for instance, the combination of land reform with generous financial assistance to the new cultivators and with an adequate supply of skilled administrative and technical manpower—not to mention the relatively high level of literacy of the rural population—has accounted in no small measure for the rapid increase in agricultural productivity in recent years. In other countries where a similar combination of measures has been applied to selected projects established in the wake of land reform, substantial increases in productivity have also been achieved. But scarcity of funds and personnel, and the complexity of the organization task, have generally precluded the nation-wide use of this approach.

Another impediment to agricultural development which is at least partly of an institutional character is the inadequacy of rural credit. The main source of such credit has been—and often continues to be—the local trader and money-lender whose exploitation of the peasants has contributed to rural poverty and stagnation. With the implementation of land reform programmes, the increased marketing of crops by peasants and the use of commercial fertilizers and other farm inputs, the need for agricultural credit has increased rapidly. Private banks have found agricultural credit costly to administer and have been unable to provide it on suitable terms to small cultivators. In these circumstances, Governments have been obliged to take major responsibility for the expansion of agricultural credit. Direct government action through the provision of funds has become more common, and in connexion with the implementation of recent plans a variety of specialized public lending agencies have been established, while the activities of general development financing agencies have been extended to agricultural credit. In recent years, international lending institutions, such as the World Bank Group and the Inter-American Development Bank, as well as various aid-giving countries, have given financial assistance to expand the financial resources of agricultural credit institutions in several countries. But in spite of a substantial expansion of agricultural credit, the resources available to credit institutions have remained inadequate and in many cases institutional credit has made no significant inroads into the activities of the local money-lender. Following the examples of China (Taiwan) and the United Arab Republic, a number of Governments have made provision in their recent plans for the strengthening of the co-operative movement in the credit field with a view to channelling the bulk of medium-term and short-term agricultural credit through the co-operative system with its numerous outlets in rural areas.

Inadequate marketing facilities have likewise been a major factor impeding agricultural progress. The need for a more effective marketing system has become the more urgent as some Governments have endeavoured to make increasing use of price policy to stimulate agricultural production and the flow of supplies to urban centres. But inadequate transportation and credit facilities, together with the shortage of qualified personnel, have made improvements in this field particularly difficult. In recent years, several Governments have established statutary marketing agencies with functions ranging from a purely advisory role at one extreme to the operation of a marketing monopoly at the other. Government intervention in marketing beyond certain regulatory activities has frequently met with opposition from political and commercial groups and, at the local level, from the established traders and money-lenders.

In several countries, including China (Taiwan), India, Republic of Korea, Pakistan and United Arab Republic, marketing agencies established by Governments have been linked with the co-operative system and have operated through it at the local level. As in the case of credit, this approach has aimed at extending organized marketing to the village level. In this, as in other areas, lack of supervisory and technical personnel has been a major bottle-neck to greater progress. In the recent plan periods, Governments have undertaken the study of marketing problems and have proceeded with the training of personnel as well as with the establishment of new marketing institutions and the framing of legislation for the regulation of marketing operations. In some countries, marketing reform has been linked with provisions for the building up of buffer stocks necessary for the stabilization of prices. This, in turn, has necessitated the construction of storage facilities. However, these construction programmes, like other investment projects in the agricultural sector, have tended to lag owing mainly to shortages of materials and funds. In India, for instance, less than half of the Food Department's target for its own storage construction under the third plan had been completed by 1965. On the other hand, the storage capacity of the state governments was expanded in the plan period to the point where under-utilization became widespread and costly to state treasuries.

PERFORMANCE IN INDUSTRY

The recent industrial performance of the countries reviewed in this chapter has been quite mixed. In comparison with past trends, there has been no general tendency towards improved performance, and relatively few countries have succeeded in achieving or exceeding their planned rates of growth. In fact, no more than four of the countries included in table 14—namely, China (Taiwan), Malaysia, Pakistan and the Republic of Korea—can be said to have achieved or surpassed their planned growth rates for industry.

Table 14. Planned and actual rates of growth in manufacturing production

(Percentage)

Country	Planned	Actual[a]	
		Plan years	Pre-plan years
China (Taiwan)	12.5	16.2	12.9
India	11.0	9.3	7.0
Malaysia	7.5	11.1	4.9[b]
Morocco	9.0	4.9	2.7
Pakistan	8.5	10.1	7.1
Philippines	10.0	5.6	9.9
Republic of Korea	11.5	15.6	16.2
Sudan	21.0	9.1	6.4
Tunisia	8.0	4.0	4.6
United Arab Republic	15.0	8.4	12.5
Venezuela	13.5	9.6	9.8

Source: See table 7.

[a] Actual growth rates based on data relating to value added in constant prices, as defined in national accounts. Plan years refer to those shown in table 7. For pre-plan years, see foot-note *c* to table 7.

[b] Manufacturing and construction.

Among other countries, the Philippines, Tunisia, the United Arab Republic and Venezuela have not only failed to achieve the planned growth rate for industry but have experienced a decline in the growth rate compared with pre-plan years. In Morocco and the Sudan, industrial expansion accelerated in the plan years although not to the extent foreseen in the plans. In both countries, the achievement of the target rate would have involved a more than threefold increase in the past rate of expansion in industrial production and may have been difficult to achieve in view of the limited availability of technical and organizational skills and of resources for investment.

In several countries, the failure to attain the planned rate of expansion has been a consequence of lagging investment in the manufacturing sector. In the Philippines and Venezuela, for instance, total investment has failed to increase at the planned rate and the share of manufacturing industry in the total has been well below that envisaged in the plan (see table 15). In Morocco, it has been reported that, in the first four years of the plan, total investment outlays on machinery and equipment—which are chiefly absorbed by industry—fell short of the planned level by more than two fifths.

Table 15. Planned and actual share of manufacturing industry in total investment

(Percentage)

Country	Planned	Actual[a]
China (Taiwan)	25	24
India:		
Total[b]	25	...
Public outlays[c]	20	20
Pakistan	26	28
Philippines	33	25
Republic of Korea[b]	28	24
Sudan	16	15
United Arab Republic[b]	27	27
Venezuela	19	13

Source: See table 7.

[a] Actual data refer to years shown in table 7.

[b] Investment in manufacturing industry includes mining.

[c] Including other developmental expenditure besides investment.

But there have also been countries where shortfalls in performance have occurred in spite of the attainment of planned levels of investment. Estimates of the relationship between new investment and increments in output are, of course, subject to a wide margin of error, and to the extent that plans are based on some assumed ratio between these two magnitudes rather than on a project-by-project appraisal of investment requirements, considerable disparities between plan targets and actual achievements may occur. But probably more important than such technical deficiencies in the formulation of targets has been the fact that projections of the growth rates to be achieved with a given level of investment have been based on the assumption that industrial capacity would be fully utilized. In fact, for various reasons, under-utilization of industrial capacity has assumed major proportions in several countries during the plan periods. In India, for instance, a sample survey[3] revealed that over one third of the factories surveyed operated at, or below, 70 per cent of capacity during the plan years up to 1964, and around 15 per cent of the factories operated at, or below, half capacity. Comparable information is not available for other countries, though there is also evidence indicating under-utilization of capacity in the United Arab Republic and Morocco. In the latter country, for instance, it has been reported that 90 per cent of industrial plants were operating at 50 to 80 per cent of capacity in 1964.

In some countries, an important cause of the under-utilization of capacity has been the poor performance of agriculture. In most developing countries, manufacturing output consists predominantly of consumer goods and intermediate products which are largely based on indigenous agricultural materials. In these circumstances, shortfalls in agricultural production reduce the supply of materials for industry as well as slowing down the growth of demand for its products. Further, lack of co-ordination between the implementation of complementary industrial and agricultural projects has sometimes resulted in factories being established before adequate supplies of the needed agricultural materials had become available.

In addition to shortfalls in the domestic production of materials, shortages of imported raw materials, semi-manufactures and spare parts have also affected the operation of industries. In India, Morocco and the United Arab Republic, for instance, acute foreign exchange scarcity has at times obliged Governments to curtail imports of essential requirements for industry, forcing factories to reduce or discontinue operations temporarily. The level of activity in manufacturing industry has also been adversely affected by failure to meet plan targets for power and transport. The full utilization of existing and newly established productive capacity has also been impeded by shortages of skilled manpower and management and supervisory personnel.

Of the four countries which have attained their plan targets for manufacturing production, China (Taiwan), Malaysia and Pakistan appear to have achieved the levels of investment envisaged in the plans. Industrial growth has, moreover, benefited from the good performance of the agricultural sector which has ensured both adequate supplies of agricultural materials and a buoyant market for industrial products. Moreover, these countries have experienced a substantial expansion in exports which has enabled them to finance the necessary imports of industrial materials and supplies. In the Republic of Korea, investment in the manufacturing sector did not attain planned levels, but there appears to have been substantial idle capacity[4] in the early 1960's. The good export performance and substantial foreign exchange receipts from United States government expenditures and donations have ensured adequate supplies of imported industrial materials for a fuller utilization of the existing and newly established capacity during the plan period.

While the expansion of capacity for the production of investment goods has been envisaged in a number of plans, most countries have tended to place the main emphasis on increasing the output of substitutes for imported consumer goods, of intermediate products and of specific items with good export prospects. In the industrially more advanced countries, such as China (Taiwan), India, Pakistan and the United Arab Republic, the scope for import substitution for basic consumer manufactures had been progressively reduced as a result of earlier industrial development, and recent plans have therefore focused primarily on industries producing intermediate products such as industrial chemicals, fertilizers, refined fuels, paper, newsprint, and metal and building materials as well as those producing certain durable consumer goods. At the same time, the creation or expansion of capacity for the production of certain kinds of electrical equipment and machinery has also been envisaged. In the less industrialized countries, the food-processing, textile and other basic consumer goods industries have continued to be stressed in plans for the manufacturing sector.

The emphasis that plans and industrial development policies have given to various branches of industry has had a significant impact on the composition of output. In India, for instance, the share of machinery and intermediate goods in total manufacturing output has risen significantly at the expense of consumer goods; the share of the latter declined by one quarter between 1960/61 and 1965/66 (see table 16). Similarly, in China (Taiwan), Pakistan,

[3] Government of India, Department of Statistics, *Monthly Statistics of the Production of Selected Industries for India for June 1965* (Calcutta, 1965).

[4] It has been estimated that in 1960 only 50 per cent of manufacturing capacity in the consumer goods sector was in operation ("Development planning in ECAFE countries in the recent past" (E/CN.11/CAEP.2/L.3), paper prepared by the Secretariat of the Economic Commission for Asia and the Far East (ECAFE) for the second session of the Asian Conference of Economic Planners, Bangkok, 19-26 October 1964).

Table 16. Composition of manufacturing output, by branch

(Percentage)

Branch of manufacturing	*China (Taiwan)*		*Pakistan*		*United Arab Republic*[a]		*India*	
	1960	*1964*	*1959/60*	*1963/64*	*1959*	*1965*	*1960/61*	*1965/66*
Metal transformation[b]	5.9	8.0	9.7	11.7	14.6[c]	17.7[c]	16.3[d]	22.0[d]
Base metals	5.9	3.5	2.3	5.7	c	c		
Building materials	5.9	5.9	3.7	3.4	3.6	3.1	37.2[f]	43.2[f]
Chemicals and petrochemicals	12.7	15.5	13.6[e]	17.3[e]	8.8	13.6		
Wood products, paper and cardboard	8.0	8.1	2.3	2.5	—	—		
Food, beverages, tobacco	39.3	34.8	13.9	14.6	31.8	28.8		
Textiles and leather goods	21.0	16.7	50.2	40.1	41.2[g]	36.8[g]	46.5[h]	34.8[h]
Miscellaneous manufactures	2.0	7.5	4.3	4.7	—	—		

Source: *Industry of Free China* (Taipei), 25 January 1967; "Growth and structure change in Pakistan's manufacturing industry, 1954-1964", *Pakistan Development Review* (Karachi), vol. V, No. 1; *Statistical Handbook of the United Arab Republic, 1962-1965* (Cairo, 1966); Government of India, Planning Commission, *Fourth Five-Year Plan—A Draft Outline.*

[a] Excluding the output of government workshops, military factories, cotton pressing mills, bakeries, tea packaging plants, printing and publishing plants.

[b] Including metal products, machinery, electrical machinery, transport equipment.

[c] Base metals included in metal transformation.

[d] Machinery only.

[e] Including oils and fats.

[f] "Intermediate goods".

[g] Excluding leather goods.

[h] "Consumer goods".

the Republic of Korea[5] and the United Arab Republic, the share of the metal-transformation, chemical and related industries has increased while those of textiles and leather goods and, except in Pakistan, that of food processing industries have declined in recent years. In other countries, the pattern of change has been less consistent. In Morocco, for instance, the most significant gains have been registered by the textile industry while the base metals and metal-manufacturing branches have lagged in spite of ambitious plans for their expansion. In the Philippines, the food-processing, chemical and metal-manufacturing branches have gained at the expense of textiles, and in Venezuela, the output of the textile and metal manufacturing industries has increased more rapidly than that of other branches of manufacturing (see table 17).

For Malaysia and Sudan, no industrial production indices are available. The plans of both countries have stressed import-substituting production of consumer goods and some basic materials, and substantial progress appears to have been achieved in the industries concerned. In Malaysia, for instance, the output of such consumer goods as soap, cigarettes and inner tubes for bicycles increased sufficiently during the plan period to meet all domestic requirements. The establishment of oil refining capacity enabled the country to reduce the share of imports in the domestic supply of refined petroleum products from 100 to 41 per cent over the plan period. The expansion of cement production has not only eliminated the need for imports, which had accounted for around 10 per cent of total consumption in 1960 but has produced a surplus for export. The Sudan,

[5] Data on the composition of manufacturing output are not available for the Republic of Korea, but the rates of increase in output by branches of manufacturing indicate shifts similar to those in the other countries. Annual growth rates between 1961 and 1965 were as follows (percentage):

Food, beverages and tobacco	1.1	Chemicals	20.5
		Base metals	22.2
Textiles	14.8	Metal products	19.3

Table 17. Average annual rates of increase in manufacturing production, by major branch

(Percentage)

Country and period	*Food, beverages, tobacco*	*Textiles*	*Chemicals*	*Base metals*	*Total products*
Morocco (1959-1964)	5.8	11.9	5.1[a]	——4.2——	
Philippines (1961-1965)	6.5	4.1	6.6	...	7.2
Venezuela (1962-1965)	7.8	11.4	3.3[b]	...	19.0

Source: *Statistical Yearbook, 1965* (United Nations publication, Sales No.: 66.XVII.1).

[a] Including rubber products.

[b] 1961-1964.

which had adopted a similar approach, is reported to have exceeded plan targets for the production of various kinds of textiles and foot-wear, refined sugar and petroleum products. Substantial progress has also been made in the production of cement and other building materials.

The extent of direct government intervention in the implementation of plans for industry has varied considerably from country to country. In the United Arab Republic, the Government nationalized virtually all organized industry in 1961; this followed the earlier nationalization of banks, public utilities and transportation. Although the Government does not directly manage the nationalized enterprises, its influence on the investment decisions of the commissions administering the enterprises is, of course, substantial. In India, the Government has assumed major responsibility for the development of the capital goods sector of industry and has participated directly in the establishment of various industries producing such intermediate goods as steel, industrial chemicals and fertilizers.

In most countries, Governments have adopted a pragmatic approach to the contributions to be made to industrial development by the public and private sectors. They have tended to participate directly in industrial projects that are highly capital intensive and technologically complex and in those considered to be essential and for which adequate private capital is not forthcoming. At the same time, Governments have also devoted substantial resources to the development of basic facilities essential to the growth of the manufacturing sector.

Outside these specific areas, the success of programmes for industrial development has depended in large measure on the effectiveness of the indirect measures employed to encourage private investment and to channel it in accordance with broad plan priorities. These measures have included the granting of tax concessions to new industries, tariff protection, the provision of credits, the establishment of industrial estates and measures to encourage foreign investment. They have been selectively used to guide investment as far as possible in accordance with plan priorities. In China (Taiwan), for instance, industries producing substitutes for imported articles of mass consumption, those producing essential industrial materials, and firms exporting half or more of their output have been singled out for special tax concessions. Malaysia has established a system under which certain industries—notably, the chemical and metal industries—are granted "pioneer industry" status which carries entitlement to tax benefits and other assistance on a priority basis. Pakistan has drawn up industrial investment schedules setting broad investment targets for various branches of industry on the basis of which credits are allocated by the development banks and priorities for the granting of tax concessions are determined. Credit facilities have also been expanded and improved through the establishment and reorganization of public credit institutions; in Pakistan this has included the establishment of a National Investment Trust for the purpose of channelling small savings into industrial investment.

The policies pursued by such countries as China (Taiwan), Malaysia and Pakistan appear to have been particularly successful in yielding results. It has to be remembered, however, that industrial growth in these countries has also benefited substantially from a relatively easy foreign exchange position. Because of buoyant exports, a substantial inflow of external capital or adequate foreign exchange reserves, it has been possible to pursue a liberal import policy; and this has ensured adequate supplies of essential industrial materials and equipment. Further, the favourable performance of agriculture has both stimulated industrial investment through enlargement of the domestic market and facilitated the expansion of industrial output through the provision of raw materials.

TRENDS AND POLICIES IN THE EXTERNAL SECTOR

In view of the dependence of developing countries on imports of investment goods and other essential commodities and services, the attainment of planned rates of growth for exports and for receipts of external capital is of great importance for the implementation of plans. Trends in foreign trade, moreover, considerably affect the growth of public revenue in most developing countries, both directly through collections of export and import duties and indirectly through the influence of export receipts on domestic income.

Since the early 1960's the export trends of developing countries in general have been comparatively favourable owing to the fairly brisk world demand for primary products. However, the various commodities, and consequently the countries which export these commodities, have benefited in differing degree from the rise in world demand. The countries included in the present review are about equally divided between those which have attained higher rates of increase in export receipts than their Governments had expected at the time when plans were formulated, and those which have failed to achieve the projected level of exports (table 18). Of course, neither good nor poor export performance has necessarily been due solely to external factors. Some countries have put particular stress on export promotion and have been able through their own efforts to improve their export position within a relatively

Table 18. Planned and actual annual rates of growth in merchandise exports

(Percentage)

Country	Planned	Actual[a] Plan years Quantum	Actual[a] Plan years Value[b]	Actual[a] Pre-plan years Quantum
Republic of Korea	27	...	43.7	—3.1
China (Taiwan)	11.5	17.5	27.0	7.4
United Arab Republic	6.5	...	3.2	2.2
Morocco	5	1.4	4.4	3.6
Sudan	4.5	3.2	2.0	8.7
Venezuela	4.5	...	2.4	7.3
Pakistan	4	5.2	9.0	0.9
Tunisia	4	...	2.2	5.7
India	3.5	4.2	4.8	1.5
Philippines	3	9.3	11.3	5.4
Malaysia	—0.5	6.4	1.2	3.8
Uganda	...	10.8	17.1	...

Source: International Monetary Fund, *International Financial Statistics,* November 1966, *Monthly Bulletin of Statistics* (Washington, D.C.), February 1967, and national development plans.

[a] Plan years refer to those shown in table 7. For pre-plan years, see foot-note *c* to table 7.

[b] Based on f.o.b. value in United States dollars.

favourable environment. In others, exports have been adversely affected by such factors as harvest failure, political unrest or the diversion of export commodities to the domestic market.

In the majority of countries, imports have increased faster than the plans had envisaged (table 19). In those countries which have exceeded the planned growth rate for the gross domestic product it was to be expected that import targets would also be exceeded. But in the countries which have failed to attain the planned over-all growth rates, the fact that imports have surpassed planned levels suggests deficiencies in either the plan estimates for import requirements or the execution of the import plans, or both. There is considerable evidence that import targets in a number of plans have been unrealistic. Experience has shown that in periods of economic expansion, imports have tended to rise as fast as or faster than gross domestic product; in other words, the income elasticity of demand for imports (as measured by the ratio of the increase in imports to that of the gross domestic product) has tended to be 1.0 or higher. In setting their plan targets, however, a majority of countries have explicitly or implicitly assumed that the import elasticity in the plan period would be less—often substantially less—than 1.0 (table 20). The development of their imports during the plan period has shown

Table 19. Planned and actual annual rates of growth in merchandise imports

(Percentage)

Country	Planned	Actual[a] Plan years Quantum	Actual[a] Plan years Value[b]	Actual[a] Pre-plan years Quantum
Pakistan	14.5	22.9	23.1	0.6
Morocco	7	0.6	5.2	—1.4
Republic of Korea	6	...	9.2	2.1
Philippines	5.5	4.4	7.2	1.4
Tunisia	4.5	...	3.9	0.8
Malaysia	4	5.7	3.9	6.9
India	3.5	7.1	4.5	8.6
China (Taiwan)	3	9.6	9.6	10.1
Sudan	2	12.8	10.6	3.5
Venezuela	2	...	7.6	4.9
United Arab Republic	—1	...	8.0	7.2
Uganda	...	...	7.5	...

Source: See table 18.

[a] Plan years refer to those shown in table 7. For pre-plan years, see foot-note *c* to table 7.

[b] Based on c.i.f. values in United States dollars.

Table 20. Planned and actual elasticities of merchandise imports[a]

Country	Elasticity implicit in plan	Actual in plan years[b]: Percentage increase in: Imports	Gross domestic product	Apparent elasticity
Pakistan	3.7	180	30	5.9
Malaysia	1.4	32	36	0.9
Morocco	1.2	4	23	0.2
Republic of Korea	1.1	45	34	1.3
Philippines	0.8	19	20	1.0
Tunisia	0.8	21	22	1.0
India	0.6	16	18	0.9
Sudan	0.4	62	24	2.6
China (Taiwan)	0.3	44	48	0.9
Venezuela	0.3	24	18	1.4
United Arab Republic	—0.2	44[c]	37	1.2

Source: See table 18.

[a] For the plan period elasticity has been calculated as the ratio between percentage increase in volume of imports and percentage increase in gross domestic product between the base year and the final year of the plan or the latest year for which data are available.

[b] Plan years refer to those shown in table 7.

[c] Value of imports deflated by index of import prices for developing countries.

that the import elasticities implicit in the plans would not be attained without more far-reaching restraints than any of these countries have applied, or without a more rapid expansion in the output of essential commodities than could reasonably have been expected to occur.

In a majority of countries deficits in the balance of payments in the plan period have been larger than in pre-plan years, but in all but two countries they were smaller than plans had envisaged. Relatively stable import prices together with some improvement in export prices and a larger increase in the volume of exports of goods and services than had been projected have enabled several countries to proceed with the implementation of plans without using external capital on the scale previously considered necessary (table 21). However, smaller than planned balance of payments deficits have not necessarily reflected basic improvements in the external balance. In some of the countries which have not attained planned over-all growth rates, smaller than planned deficits have been to some extent a consequence of smaller plan outlays. Furthermore, in some countries the balance of invisibles was more favourable than anticipated.

Measures to expand exports

While export diversification has generally been a major long-term goal of development policy, in the relatively short period of a single medium-term plan the over-all export performance has necessarily depended in large measure on external factors affecting traditional export commodities. Most of the countries reviewed in this chapter have established targets for their traditional commodity exports and

Table 21. Planned and actual deficit in balance of payments on current account[a]

(Annual average in millions of dollars)

Group and country	Planned	Actual[b]: Plan years	Pre-plan years
Countries where actual deficit has been greater than planned:			
Sudan	43	67	3
Tunisia	89	128	—7
Countries where actual deficit has been smaller than planned:			
China (Taiwan)	102	67	109
India	1,113	886	405
Republic of Korea	264	226	254
Malaysia	88	32	16
Pakistan	698	367	169
Philippines	178	—92	43
United Arab Republic	367	229	66
Venezuela	45	—235	—224

Source: International Monetary Fund, *Balance of Payments Yearbook*, vols. 17 and 18 (Washington, D.C.), and national development plans.

[a] Balance of payments on current account refers to balance of goods, services and private donations. Minus sign indicates surplus.

[b] Plan years refer to those shown in table 7. For pre-plan years, see foot-note *c* to table 7.

they have introduced some measures to promote export sales. But the main emphasis of plans for the external sector has been on measures to accelerate the process of export diversification. Thus, as table 22 shows, Pakistan has sought to reduce the share of its major exports from 80 to 75 per cent of total exports within a single plan period, and the Sudan and the United Arab Republic have planned to achieve even more substantial shifts in the commodity composition of their exports. Similar shifts were implicit in other plans, though no specific targets were announced. It appears from the limited sample presented in table 22 that substantial progress has in fact been made towards export diversification, though the figures for the actual shares of major export commodities in 1965 may overstate the progress to the extent that reductions in the shares of these commodities may have resulted from shifts in the relative prices of major and minor export products in favour of the latter. But there is no doubt that export diversification has contributed to the relatively good export performance of a number of countries in recent years. In particular, several of those reviewed here have made a major effort to promote exports of manufactures and to establish industrial plants which would enable them to export some of their major export commodities in more processed or semi-manufactured form.

Table 22. Planned and actual share of major export commodities in total exports

(Percentage)

Country and commodity	Planned share: Base year of plan	Planned share: Final year of plan	Actual share: 1965 or final year of plan[a]
India			
Tea, cotton and jute manufactures	53	...	49
Pakistan			
Cotton, jute and manufactures	80	75	74
United Arab Republic			
Cotton, rice	69	58	64
Venezuela			
Petroleum	93	91	91

Source: See table 18.
[a] 1964 for Pakistan and United Arab Republic.

Manufactures and semi-manufactured products have indeed come to account for a significant and increasing proportion of the exports of several countries:

SHARE OF MANUFACTURES[a] IN TOTAL EXPORTS

(Percentage)

Country	Base year of plan: Total manufactures	Base year of plan: Total (excluding textile manufactures)	Latest yearof plan[b]: Total manufactures	Latest yearof plan[b]: Total (excluding textile manufactures)
India	43	8	45	11
Pakistan	28	9	35	14
China (Taiwan)	15	7	34	24
Republic of Korea ..	15	13	49	40
United Arab Republic	12	4	15	4

[a] Sections 5-8 of *Standard International Trade Classification* (SITC).
[b] 1965, except for China (Taiwan), Pakistan and United Arab Republic where data refer to 1964.

A particularly promising development in several countries has been the increase in the export share of manufactures other than textiles since the scope for expanding exports of textile manufactures has been limited both by the relatively slow growth of world demand and by the fact that exports from low-cost producers have been restricted by various means in the interests of producers in some of the major importing countries. China (Taiwan), for instance, has developed an important export trade in plywood, cement and plastics. It has also succeeded in establishing itself as an exporter of iron and steel and of certain kinds of machinery; these accounted together for almost 5 per cent of total exports in 1964. Similarly, in the Republic of Korea, plywood and veneers came to contribute almost 10 per cent of total export receipts in 1964, and iron, steel and machinery for another 4 to 5 per cent. In Pakistan, which has continued to rely heavily on exports of textile manufactures, products such as cement, paper, petrochemicals and miscellaneous manufactures have assumed increasing importance in its exports. In India, domestic requirements have apparently not permitted major increases in exports of basic industrial goods such as iron, steel and cement, but exports of machinery and metal manufactures, though still small, expanded over the period of the third plan; and exports of miscellaneous manufactures more than doubled in the plan years.

Measures to expand exports of manufactures have addressed themselves to three kinds of problems: the pressure of domestic demand for manufactures and the greater profitability of sales to the domestic market; high production costs and inadequate quality control in some industries, and the development of export outlets. The promotion of exports has also involved the creation and strengthening of institutions concerned with trade matters.

In developing countries, the growth of manufacturing industries has usually been directed towards import substitution and has been geared to the domestic market. Since many of the manufactures continue to be in short supply domestically, the promotion of exports usually requires measures to limit domestic demand or to restrict domestic sales, which are often more profitable to producers than sales in the more competitive export markets. Fiscal and other measures to curb domestic consumption of products with good export prospects have therefore formed an important part of export promotion policies in such countries as China (Taiwan), India and Pakistan.

A second set of policies has been the creation of specific incentives to export, especially where industries fostered behind high protective tariffs have encountered difficulties in meeting competition in export markets. Incentives have taken such forms as tax concessions to manufacturers making a proportion of their output available for export, the allocation on a priority basis of foreign exchange for imports of materials used in the manufacture of products for export and the partial or total exemption of exporters of specific products from the obligation to surrender foreign exchange receipts to the Government.

An incentive which has been widely used has been the refund of import duty paid on materials used in the manufacture of certain export products. In addition, some countries, including India, have granted refunds of various indirect taxes levied at the different stages of production of a manufacture destined for export. Rebates on direct taxes have also been granted to firms exporting a specified proportion of their output. India, for instance, adopted a system of tax credit certificates in 1966 under which exporters of specified products are entitled to tax rebates on amounts of income equivalent to a proportion of their export proceeds. Similar provisions have been in effect for some years in China (Taiwan) and the Republic of Korea.

In countries where foreign exchange and import restrictions have been in effect, schemes providing for the retention by the exporter of a proportion of export proceeds have proved very effective in stimulating exports. Pakistan, for instance, introduced an export bonus scheme under which exporters of specified products—manufactures as well as certain other commodities—are permitted to retain 20-30 per cent of their export proceeds which they may either use to finance imports of specified items for their own use or sell at a premium in the free foreign exchange market. The Pakistan Planning Commission has estimated[6] that exports of products covered by the scheme increased by two thirds between 1959/60 and 1964/65. The extension of the scheme to receipts from invisibles has also produced highly satisfactory results. A scheme based on the same general principle has also been used in the Republic of Korea with good results. This scheme differs from that of Pakistan in that the exporter may use the retained export proceeds for imports of commodities which are normally subject to restrictions and which can be sold on the domestic market at a substantial profit.

Measures to strengthen foreign trade institutions have included the establishment of export promotion committees or boards, the creation or broadening of official export credit and insurance facilities, and provisions for standardization, grading and quality control of export products.

While specific measures to stimulate exports have contributed to the good export performance of several countries, general policies to ensure an adequate expansion of domestic production have been no less important to the promotion of exports. It was noted, for instance, in a report of the Planning Commission of Pakistan that:

> "The sharp increase in the country's exports was brought about by a number of factors, the most important of which was increased agricultural production.... The production targets, as originally estimated in the second plan, were exceeded specially in commodities like cotton, rice and miscellaneous primary commodities which had considerable export potential".[7]

Import policy and import performance

Many of the countries reviewed in this chapter have maintained fairly stringent import and foreign exchange controls during the plan years. In principle, they have given priority in their import policy to capital goods, essential materials for industry and basic consumer goods which were not available from domestic sources, while imports of other consumer goods have been restricted with varying degrees of severity according to the availability of foreign exchange. Since the period of recent plans has witnessed improvements in the export receipts of several countries, import restrictions have been eased in a number of cases. This has given an upward impetus to imports generally, and in particular to imports of consumer goods. In many instances, the tendency for imports to rise more strongly than projected has arisen from unplanned increases in imports of consumer goods. To some extent these "unplanned" increases have been a reflection of the fact that targets for imports of consumer goods had been based on very crude estimates or had been determined without reference to the prospective growth of consumption

[6] Government of Pakistan, *The Third Five-Year Plan (1965-70)*.

[7] *Ibid.*

or the possibilities of expanding the domestic output of import substitutes.

In several countries, increased import requirements for food-stuffs have also contributed to the unplanned advances in imports of consumer goods. Failure to attain the food production targets in India, the Philippines, the Republic of Korea, the United Arab Republic, and elsewhere has necessitated larger food imports than had been anticipated. To the extent that these imports have been covered by commodity aid—chiefly from the United States under Public Law 480—no foreign exchange expenditure has been involved. In many cases, unforeseen increases in imports of other consumer goods have also occurred: in fact, in some countries such imports have increased no less than imports of capital goods and industrial materials, as is implicit in the data shown in table 23. For instance, the share of non-food consumer goods in total imports has risen in China (Taiwan), Malaysia, Morocco and the Philippines and has declined very little in India, Tunisia and Venezuela. In each of these countries the plan had envisaged a substantial reduction in the share of consumer goods in total imports.

Table 23. Changes in the composition of imports[a] in the plan period

(Percentage)

Country and period	Consumer goods: Total	Consumer goods: Food	Consumer goods: Other	Intermediate products	Capital goods
China (Taiwan)					
1960	15	9	6	48	37
1964	20	10	10	51	29
India					
1960/61	25	19	6	28	47
1964/65	25	20	5	23	52
Malaysia[b]					
1960	51	30	21	30	19
1964	52	30	22	23	25
Morocco					
1960	51	22	29	26	23
1964	51	28	23	26	23
Pakistan[c]					
1960/61	33	20	13	29	38
1964/65	24	15	9	28	48
Philippines					
1961	31	13	18	26	43
1964	33	16	17	24	43
Republic of Korea					
1961	33	13	20	49	17
1965	23	14	9	55	22
Sudan					
1960	60	17	43	18	23
1965	55	24	31	17	28
Tunisia					
1961	52	28	24	19	30
1965	36	14	22	20	44
United Arab Republic					
1959	36	25	11	32	32
1964	33	27	6	32	35
Venezuela					
1962	37	12	25	17	46
1964	36	13	23	16	48

Source: United Nations, *Yearbook of International Trade Statistics*, and national sources.

[a] Grouped according to SITC: consumer goods, 0, 1, 6 (except 67-69), 732.1, 8 and 9; intermediate goods, 2-5; capital goods, 67-69 and 7 (except 732.1).

[b] Federation of Malaya only.

[c] Based on data from national sources; commodity classification is not strictly comparable with that for the other countries included in the table.

The share of raw materials and intermediate products in total imports has generally not increased significantly and, in some instances, it has declined. In some countries, such as China (Taiwan) and Pakistan, where the rate of growth in industrial production has been high, such imports might have been expected to account for a rising proportion of total imports; the good performance of domestic primary production, and of agriculture in particular, has probably helped to limit import demand for these industrial inputs. In other countries, the share of raw materials and intermediate products in total imports has not increased, more because of the lack of foreign exchange than because demand has been satisfied from domestic sources. In India and the United Arab Republic, for example, the high priority given to imports of capital equipment, together with the limited scope for further reductions in imports of consumer goods, has meant that any tightening of foreign exchange restrictions has tended to fall on imports of raw materials and intermediate products. This has adversely affected the ability of these countries to operate existing industries at full capacity.

In a few countries, including China (Taiwan), Pakistan, and the Republic of Korea, major steps were taken towards liberalizing imports, especially of industrial materials, replacement parts and other requisites. The import liberalization programme of Pakistan, for instance, was launched at the beginning of the second plan with a system of "automatic licensing" under which a large number of industrial materials and spare parts could be imported as soon as the importer had utilized the previous licence. The number of items included in this programme has been progressively increased so that by the end of the plan period imports of a wide range of basic industrial and agricultural requirements had become readily available. These measures were accompanied by fiscal policies to check increases in demand and undue substitution of local materials and manufactures. Import liberalization has formed part of the Pakistan Government's programme to place increased reliance on the operation of the market in the execution of its development programme.

Aid policy and the financing of import balances

It has been noted earlier that, in some cases, the unavailability of external aid and capital on acceptable terms has accounted for the fact that balance of payments deficits have been smaller than had been envisaged in plans. In order to understand the nature of the problem it is necessary to consider the plan targets for external financing in relation to both the amount of financing obtained in the pre-plan years and the amount of aid and capital which the developed countries and international institutions have made available to developing countries in the first half of the 1960's. The majority of the countries shown in table 21 had envisaged in their plans that the annual inflow of external resources during the plan years would be a multiple of its level during the latter part of the 1950's. Their planned annual deficits amounted in the aggregate to almost $3 thousand million compared to actual deficits of some $800 million in the years preceding the plans. The assumption that the flow of international resources to developing countries would increase sufficiently in the 1960's to finance annual deficits two or three times as large as those of the late 1950's may not have seemed unrealistic at the time when recent plans were being formulated, in view of the rapid expansion in the flow around the turn of the decade. However, these expectations were disappointed by subsequent developments. In the first half of the 1960's, the average net annual flow of aid and long-term capital from developed countries and multilateral agencies to all developing countries was only 25 per cent larger than the average for the preceding five-year period. In these circumstances, it became necessary to scale down plan targets for balance of payments deficits. Several major aid recipients, including India, Pakistan and the United Arab Republic, none the less succeeded in finding the necessary resources to finance substantially increased annual deficits; these were more than twice as large as those of the pre-plan years.

In addition to the problem of the inadequate supply of external capital in relation to targets, the composition of aid and some of the non-financial terms imposed by the lenders have also proved a handicap to the realization of balance of payments targets.[8] A significant proportion of the available external resources has consisted of food aid which can be used only to fill gaps in the supply of specific food-stuffs. Furthermore, a substantial part of cash aid has been available only for the financing of specific investment projects. Over the years, the number of large infrastructure projects for which such aid has been most readily available has diminished in some of the countries which are being reviewed in this chapter, either because the most important projects have already been completed, or because the emphasis of development plans has shifted to less capital-intensive investments for which project assistance is not suitable. Although the availability of non-project aid from various sources has increased, the supply has remained insufficient to meet the growing demand. Finally, in a number of the more industrialized countries such as China

[8] For a more detailed discussion of these questions, see *World Economic Survey, 1965: Part I—The Financing of Economic Development* (United Nations publication, Sales No.: 66.II.C.1) and E/4371 and E/4375.

(Taiwan), India, Pakistan and the United Arab Republic, there has been a growing need for funds to finance imports of industrial materials and spare parts rather than of capital equipment. But until fairly recently, assistance on concessionary terms has not been available for such purposes on a scale commensurate with needs. In conclusion, it should also be noted that the level of indebtedness has risen rapidly in several countries and growing debt servicing obligations have forced some of them to become more cautious in their international borrowing.

RECENT PROGRESS IN THE MOBILIZATION OF DOMESTIC RESOURCES

A progressive increase in the level of investment is a major aim of policy in most developing countries. While plans have generally assumed that a net inflow of foreign capital would make a significant contribution towards raising levels of investment, they have necessarily placed main reliance on the additional resources which could be released through greater domestic saving. Policies towards this end have been specified in most plans, though often only in very broad terms.

In several countries, the levels of domestic saving realized over recent plan periods have represented a perceptible improvement over past performance (see table 24). In China (Taiwan), India, Pakistan, the Philippines and the Republic of Korea, there has been a distinct upward movement in the share of domestic saving in gross domestic product; and, apart from the Republic of Korea, the actual level of domestic saving has either matched or exceeded the plan target. In the United Arab Republic also, although data are available for only one pre-plan year, it seems that the recent level of domestic saving has also represented an improvement over past performance. It should be noted, however, that although the share of domestic saving in gross domestic product has risen in these countries, the rate of increase in domestic consumption has not necessarily been lower than elsewhere. It might have been expected that in countries with favourable saving performances more rigorous policies to restrain domestic consumption would have been pursued. It is certainly true that an increase in the share of domestic saving in gross domestic product implies an offsetting decline in the share of consumption, but this need not mean that the rate of increase in consumption has been low. In fact, two of the countries in which the share of domestic saving in gross domestic product has increased significantly—namely, China (Taiwan) and the Republic of Korea—also number among the countries with the highest rates of growth in total domestic consumption (see table 25). Because of unusually high rates of increase in total output, these countries have found it possible both to permit absorption of a rising proportion of domestic output in investment and to support a substantial rate of increase in consumption. It is only in India that a low rate of increase in total output, occasioned mainly by the very poor performance of agriculture, has been accompanied by the allocation of a rising proportion of resources to investment. While data are not available, it is clear that the rate of increase in total consumption must have been small. The overriding reason, however, has been the lack of expansion in food production rather than deliberate restraint on the growth of consumption.

Table 24. Share of gross domestic saving in gross domestic product over plan and pre-plan periods; annual average

(Percentage)

Country	Actual[a] Plan years	Actual[a] Pre-plan years	Planned
China (Taiwan)	15.5	10.5	13.0
India	9.5[b]	7.0	9.0
Malaysia	16.5	20.0	12.0
Morocco	10.0	15.0	19.0
Pakistan	10.5	6.5	6.5
Philippines	15.5	8.5	14.0
Republic of Korea	7.0	4.5	10.5
Sudan	10.0	9.5	8.0
Tunisia	9.5	9.5	21.0
United Arab Republic	12.5	...	17.0
Venezuela	23.0	22.5	20.0

Source: United Nations, *Yearbook of National Accounts Statistics, 1965* and questionnaire 1966; Bert Hansen, *Planning and Economic Growth in the United Arab Republic (Egypt)*; and national development plans.

Note: Data are in current prices, except for India where they are in 1960/61 prices. Definitions of gross domestic product and gross domestic savings generally conform to those in plans. For India, data refer to net domestic savings and national income.

[a] Plan years refer to those shown in table 7. For Pakistan and the United Arab Republic, pre-plan data refer to base year of plan only; for other countries, pre-plan years refer to five years preceding first year of plan.

[b] Average of two terminal years of plan period.

Among the other countries shown in table 24, the share of domestic saving in gross domestic product over recent plan periods has either not increased significantly in comparison with pre-plan years or has actually declined. In Malaysia, Sudan and Venezuela, however, the share of domestic saving over the plan period has been higher than expected in plans. The targets for domestic saving had been scaled downwards in these countries mainly because the rate of growth in export income had been expected to be lower than in pre-plan years.. Since foreign trade bulks large in the economies of these countries and export earnings are channelled through large private concerns or state marketing boards with relatively high propensities to save, variations in

Table 25. Planned and actual annual rates of growth in total, public and private consumption[a]

(Percentage)

Country	Total		Public		Private	
	Planned	Actual	Planned	Actual	Planned	Actual
China (Taiwan)	7.0	7.6	...	3.0	...	8.9
Ecuador	5.4	6.3	4.9	8.9	5.5	5.9
India	4.9	...	...	...	...	...
Jamaica	5.1	5.1	...	4.6	...	5.1
Malaysia	3.7	6.2	5.6	10.0	3.4	5.3
Morocco	4.3	2.9	6.4	4.7	4.3	2.6
Pakistan	3.4	5.5	...	10.4	...	5.0
Philippines	5.5	3.4	5.5	3.4	5.5	3.4
Republic of Korea	3.1	6.6	4.7	1.2	2.8	7.5
Sudan	4.9	5.0	6.5	10.6	4.7	4.3
Tunisia	3.6	4.5	...	5.1	...	4.4
United Arab Republic	4.9	...	5.1	11.8	4.9	4.5
Venezuela	6.0	8.8	2.7	8.4	6.6	8.9

Source: United Nations, *Monthly Bulletin of Statistics; Yearbook of National Accounts Statistics* and questionnaire; International Monetary Fund, *United Arab Republic—A Survey of Developments during the First Five-Year Plan;* and Organisation for Economic Co-operation and Development, *National Accounts of Less Developed Countries.*

[a] Data are in constant prices. For Malaysia, Morocco and Venezuela, data deflated by cost of living indices. Actual data cover years shown in table 7.

rates of growth of export income considerably affect their level of domestic saving at prevailing prices. In the event, the actual growth of export income in Malaysia turned out to be better than expected, with favourable consequences for the level of domestic saving. In the other two countries, export earnings increased even less than expected, and the increase in domestic saving above the planned level must be ascribed to other factors.

In the remaining countries shown in the table, namely, Morocco and Tunisia, the actual share of domestic saving in gross domestic product remained substantially below the ambitious targets specified in their plans. In Morocco, the share during the plan period was actually lower than in the pre-plan years. Following the large-scale outflow of expatriates and capital which took place in the 1950's, the economy has failed to regain its past level of saving.

The interesting question concerning these recent changes in the performance of domestic saving is how far these have been influenced by government policies. This is, of course, an extremely difficult question to answer, particularly within the limited scope of a report of this nature. The actual performance of domestic saving is heavily influenced by other factors besides government policies. It has just been pointed out, for example, that changes in the level of export income are an important determinant in some countries. Further, it must always be borne in mind that an increase in the share of domestic saving in gross domestic product may at times be the result not of measures and events which have strengthened the propensity of the community to invest and save but of resort to the inflationary financing of investment; and the consequential price increases and shifts in income distribution, while sometimes permitting closer realization of targets for domestic saving, hardly conform with the other aims of most plans to maintain price stability and bring about a more equitable distribution of income. Moreover, as experience has shown, the scope for increasing the saving ratio in this way is limited, and indeed attempts to finance investment through inflationary processes have frequently proved to be self-defeating. In fact, domestic prices in a number of the countries under review have increased over recent plan periods, sometimes at rates of 5 per cent *per annum* or more. In the Republic of Korea, for example, wholesale prices rose at an annual average rate of about 18 per cent over the plan period. At the same time, the share of wages and salaries in national income declined from about 37 per cent at the beginning of the period to about 32 per cent at the end. This combination of circumstances strongly suggests that actual growth of investment was made possible through inflationary financing and the redistribution of income to higher-income groups.

While such complications obscure the effects which government policies to promote investment and saving may have had, one point can at least be made with some confidence. This is that, in so far as such policies have contributed to the growth of investment and saving, their influence has been exerted mainly on private investment and saving. As discussed later, in most of the countries reviewed the evidence suggests that public saving has not increased or has declined in recent years; and in countries where the level of total domestic saving has risen, it has therefore generally been private saving which has accounted for the increase. Again, there have been certain exceptions. In the United Arab Republic, in particular, the extension of public ownership over large areas of productive activity has necessarily placed the main burden of obtaining increased domestic saving on the public sector. Enactment of this policy, in fact, very substantially changed the pattern of domestic saving from that which had been expected in the plan; the plan assumed that as much as 77 per cent of total domestic saving by the end of the period would be derived from private sources whereas, as it turned out, public saving accounted for about 70 per cent.

Measures to promote private saving

The policies pursued in regard to private saving have usually fallen into two groups—those geared directly towards the promotion of personal saving and those intended to encourage private saving by strengthening the incentive to invest in the private sector. While the approaches towards private investment have varied, all countries have sought, in some degree, to encourage the growth of personal saving. In this regard, an important form of personal saving which has made some progress during the period under review has been contractual saving. Schemes for contractual saving, whether voluntary or compulsory, have been initiated or broadened by a number of Governments in the recent past. In the United Arab Republic, for example, the number of contributors to the social insurance scheme amounted to about 1.6 million persons in 1963/64, having approximately doubled since 1959/60. As a percentage of total tax revenue, inclusive of social security contributions, these contributions rose from 11 per cent in 1959/60 to 29 per cent in 1964/65. In several other countries, the coverage of social security schemes has similarly been broadened. The period reviewed saw, for instance, the introduction of a compulsory provident fund scheme for central government employees in India and a national insurance scheme in Jamaica which allows for the voluntary participation of self-employed persons. In addition, most Governments have continued to foster the spread of such new institutions and instruments as rural savings banks, credit co-operatives and stock exchanges which facilitate personal saving. Since saving habits respond mainly to improvements in the level of living, however, it may be doubted whether these measures can have had a very great effect on the aggregate level of saving. Their main importance lies rather in promoting the redirection of private saving into more productive forms of investment from such less productive uses as gold hoarding, speculative inventory accumulation and luxury housing.

A marked improvement in the level of private saving over a relatively short period of five to ten years invariably arises from an increase in private investment. In most of the countries under review, Governments have encouraged private investment through a variety of familiar measures, such as tax concessions, tariff protection, the provision of loans and the strengthening of the economic infrastructure. Probably the most important influence of government on private investment and saving, however, has been exerted not so much through specific measures to encourage investment as through the general economic conditions which policies at large have helped to create. It is where favourable general economic circumstances have combined with specific measures conducive to investment that private activity has received its greatest impetus. For instance, two of the countries in which private saving has increased strongly are China (Taiwan) and Pakistan, and in both countries a number of factors have contributed to this situation. The relatively high rates of growth in total output and a steadily expanding market have created a favourable climate for private investment. At the same time, the scope for new import-substituting production in small and medium-scale industries has remained considerable. Further, there has been a strong growth in export receipts supplemented by a substantial inflow of external assistance. Because of the expanding inflows of imported materials, existing industrial capacity has been more fully utilized in most years; and additions to capacity have not been seriously impeded by an inability to finance imports of capital equipment. Such circumstances, together with favourable fiscal and protective policies, have led to an upsurge in private investment activity and a related increase in private saving. In Pakistan, for example, it has been estimated that, in the modern industrial sector, savings out of profits after taxes have averaged about 75 per cent in recent years.[9]

Public revenue and expenditure

In the plans of most of the countries reviewed in this chapter, an increase in the level of public saving has usually been expected to contribute to the expansion of total domestic saving. Since Governments can directly influence the level of public saving through measures to raise revenue and to control current expenditure, such action has generally been

[9] Khadija Haq and Moinuddin Baqai, "A study of savings in the corporate sector in Pakistan", March 1966 (mimeographed), quoted in "Foreign assistance: Some critical issues", by Mahbub ul Haq; paper presented to United Nations Interregional Seminar on Development Planning.

assigned a central role in policies to promote saving. In most countries, however, planned increases in the level of public saving have failed to materialize. While quite a number of countries have succeeded in raising the level of current revenue, these gains have generally been accompanied by greater increases in current expenditure than assumed in plans.

The evidence suggests that, in most of the countries under review, fairly vigorous efforts have been made to raise tax revenue over recent plan years. In several countries, the level of tax revenue, when expressed as a percentage of gross domestic product, has been appreciably higher than in the years immediately preceding plan periods (see table 26). It is true that in such countries as Malaysia, Sudan and Venezuela, where trends in foreign trade are a major determinant of tax receipts, there has been little change in the level of revenue. But it is only in China (Taiwan) that a decline in tax revenue as a percentage of gross domestic product has taken place.

Table 26. General government tax revenue and consumption expenditure as percentages of gross domestic product; annual averages of pre-plan and plan years[a]

Country	Tax revenue		Consumption expenditure	
	Pre-plan	*Plan years*	*Pre-plan*	*Plan years*
China (Taiwan)	16.2	14.4	19.5	18.1
India	8.9	12.1	9.2	12.1
Malaysia[b]	17.6[c]	16.9[c]	14.2	15.0
Pakistan	7.0	9.1	7.9[d]	9.8[d]
Philippines	10.6[e]	12.1[e]	8.7	9.8
Republic of Korea	9.5	9.7	13.4	11.5
Sudan	8.8	9.0	8.0	10.9
Tunisia	19.4	21.9	16.8	16.8
Uganda	11.6	14.8	12.9	17.4
United Arab Republic	11.4	14.3	18.9	23.3
Venezuela	16.5	16.3	13.5	13.1

Source: United Nations, *Statistical Yearbook; Yearbook of National Accounts Statistics* and questionnaire; Organisation for Economic Co-operation and Development, *National Accounts of Less Developed Countries,* and national sources.

[a] Data for tax revenue generally refer to general government tax revenue. For India, Malaysia and Pakistan, data refer to central and state governments; and for Sudan, Uganda and the United Arab Republic to central government.

Data for consumption expenditure generally refer to general government consumption expenditure. For India and Pakistan, data refer to central and state governments current expenditure; and for Uganda and the United Arab Republic to central government current expenditure.

Gross domestic product at market prices is used wherever data are available. Data for Pakistan and Uganda refer to gross domestic product at factor cost, for United Arab Republic, gross national product at market prices, and for India, to national income.

Pre-plan years generally refer to five years preceding first year of the plan. For Tunisia, two years; for United Arab Republic, base year only; and for Venezuela, three years preceding the plan.

[b] Federation of Malaya only.

[c] Including other receipts.

[d] Including interest on public debt.

[e] Including current transfers from household and private non-profit institutions.

In some countries, such as India and Pakistan, international tensions created conditions which facilitated the imposition of additional taxes. But the will to raise taxes appears to have been quite widespread among the countries under review. Several countries have lowered the exemption limits on personal income-taxes and have increased the tax rates on corporate incomes. Consumption taxes have also been extended or raised in a number of countries. And in some instances, such as Tunisia, the agricultural tax system has been strengthened. Of course, these increases have been partially offset by the various tax concessions mentioned elsewhere in this chapter, which have been granted to promote investment or exports. But the reform of tax systems to improve their revenue-yielding capacity none the less appears generally to have made some progress.

Since Governments in many developing countries have assumed responsibility—either directly or through the creation of public enterprises—for a wide range of economic activities, there has also been considerable opportunity for increasing saving in the public sector by other means besides taxation. Most plans called for revision of the pricing policies of public enterprises and of the economic services directly provided by Governments in order to enlarge their contribution to public saving. But progress in this area appears to have been generally much slower than in the field of taxation. In a number of countries, such as India, Jamaica, Pakistan and the United Arab Republic, the prices charged for such economic services as irrigation have been held low as a matter of deliberate policy in order to encourage their greater use. At the same time, however, little has been done to ensure that, where no special reason prevails for subsidizing output, the prices charged by public enterprises are adequate enough to allow them to contribute to domestic saving.

Although total revenue has generally increased as a percentage of gross domestic product, thanks mainly to quite vigorous fiscal measures, it has usually been accompanied by an increase in current expenditure of much the same magnitude. This can be seen readily enough from comparison of the data presented in table 26 on government consumption expenditure with those relating to tax revenue. While tax revenue and consumption expenditure are not identical with total revenue and total current expenditure, they are sufficiently large components to serve as broad indicators of trends in the latter.

As pointed out in an earlier chapter, there has been a widespread tendency among countries to underestimate the likely growth in current expenditure when plans for the public sector have been drawn up. The stress in development programmes has usually been placed on the need to increase public investment, and in order to help finance this additional investment it has been planned to restrict the future growth in current expenditure. Little attempt has consequently been made to appraise carefully the increase in current expenditure which is likely to be needed over the plan period. Further, the effects of investment programmes in generating future requirements for additional recurrent expenditure have also tended to be neglected. Aside from these common reasons, current expenditure in some countries such as India, Pakistan and the United Arab Republic has also increased beyond plan targets because of an expansion in defence expenditure. And it is also true that, particularly when public revenue has increased, many Governments have not been able to withstand the pressure to expand public social services more rapidly.

SUMMARY

An appraisal of the experience of a selected group of countries which have been engaged in implementing development plans in the years 1960 to 1965 shows significant improvements in the performance of a number of cases. Of the twelve countries which have been reviewed all but two have recorded higher growth rates in gross domestic product than had prevailed in the latter part of the 1950's. Moreover, six countries—China (Taiwan), Malaysia, Pakistan, Republic of Korea, Sudan and Uganda—have exceeded the growth targets envisaged in their plans.

Improvements in the performance of agriculture have played a significant part in accelerating growth, although in a number of countries these improvements have not been as great as the plans had envisaged. This has been most notably the case in some major food-deficit countries such as India, Morocco and the United Arab Republic, which have failed in their efforts to reduce their dependence on imported food-stuffs. But a few countries have succeeded in expanding agricultural production at higher rates than they had planned. Although climatic factors have inevitably influenced agricultural production, vigorous measures to extend the area under cultivation and to increase the productivity of the land have contributed significantly to the improved performance in agriculture. In this connexion, a notable development has been a widespread and substantial increase in the use of fertilizers. The role of institutional deficiencies in preventing progress in the agricultural sector has come to be better understood and several countries have addressed themselves to problems of land reform and the improvement of agricultural marketing and credit systems with greater vigour.

Performance in industry in relation to plan targets has been rather uneven although growth rates have generally been substantially higher than in agriculture. In some countries, industrial production has been hampered by inadequate supplies of domestic agricultural materials and shortages of imported materials which have resulted from foreign exchange scarcity.

Although world demand for primary products has been fairly buoyant since the early 1960's, not all of the countries reviewed have benefited from this development. But favourable world market conditions have enabled a number of countries to increase their exports at a substantially greater rate than they had envisaged in their plans. This development has contributed in no small measure to the vigorous pace of development in China (Taiwan), Malaysia, Pakistan and the Republic of Korea.

Imports have generally increased more rapidly than planned. However, in many cases the higher rates of increase have been in line with higher rates of growth of output. Balance of payments deficits have generally not been as large as Governments had expected. This has been partly due to favourable developments in the export sector, and in some cases to improvements in the service balance.

In most countries, the share of investment in gross domestic product has risen during recent years, and more than half of the countries reviewed have succeeded in raising the level of domestic saving. Improvements in the performance of domestic saving have mainly reflected higher levels of private investment and saving. While public revenue has generally increased in relation to gross domestic product as a result of efforts to increase taxes, corresponding increases in public current expenditure have tended to prevent a significant expansion of public saving.

B. *Some aspects of plan implementation in centrally planned economies*

INTRODUCTION

The following chapters review certain aspects of the experience of the centrally planned economies which may be relevant to the problems of plan implementation in developing countries discussed in the preceding chapters; they are not intended to provide a comprehensive account of the methods of preparation and implementation of development plans in the centrally planned economies.[1]

Despite the fact that the methods of planning and of implementation of plans adopted in the centrally planned economies were closely related to the political and social conditions prevailing in those countries, their impact on planning in countries with other economic and social systems was quite considerable. This influence was not confined to a general recognition of the advantages of development planning but was also reflected in the introduction in several countries, with various modifications, of certain methods which were first tested in the centrally planned economies. Mention could be made in this context, for instance, of the adoption of five-year plans, the use of commodity balances, the internal organization of the planning agencies and their relations with executive and legislative bodies, and, to some extent, the verification of the feasibility of provisional aggregate targets through consultations with operating units.

It is obvious that no similar transfer of experience was possible in the field of plan implementation. As long as the implementation of plans in the centrally planned economies was largely achieved by administrative order, very few aspects of this experience could be relevant to the solution of the problems faced by countries with predominantly market economies.

The changes in methods of planning and management that are taking place in the centrally planned economies, however, tend to enlarge the area of common interest considerably, and to make the experience of the centrally planned economies in the field of plan implementation increasingly relevant to the solution of problems faced by countries with different economic and social systems. In spite of the differences that still affect methods and policies of both planning and implementation, developments in both groups of countries have created conditions for a much broader interchange of experience and its adaptation to different national circumstances.

It needs hardly to be stressed that the conditions under which the centrally planned economies developed their planning system were very different from those in effect in most of the developing countries at the present time. Clearly, the most important difference was in the sphere of economic and social institutions, which had a decisive impact on methods of planning and of plan implementation. It is often overlooked, however, that these differences notwithstanding, there is a great deal of similarity in other conditions, which also have considerable bearing on planning and development policies in developing countries and in the centrally planned economies.

This is clearly indicated by the fact that in the early stages of their planned development at least, the main economic problems facing the centrally planned economies and the general economic objectives of their plans were stated in terms almost identical with those used by the developing countries: the elimination or reduction of the gap between their level of development and that of the developed market economies, by means of an acceleration of the over-all rate of growth, a substantial increase in the rate of accumulation, rapid industrialization and profound changes in economic structure. The foreign trade problems faced by the centrally planned economies were also in many respects similar to those of the developing countries. This was particularly true with respect to the Soviet Union before the Second World War.

The importance of these problems and objectives to the elaboration of methods of planning and plan implementation is clearly indicated by the fact, which will be discussed below, that changes in these conditions have been reflected in substantial modifications of these methods. This in no way alters the fact that the impact of such problems on the planning system was clearly outweighed by the influence of the political and social conditions prevailing at the time of its introduction. Moreover, decisions relating to methods of planning and plan implementation were also influenced by the state of knowledge regarding various indirect means of influencing economic growth, which was at the time very inadequate. The

[1] In the context of these chapters the term centrally planned economies covers only the eastern European countries of this group. These chapters do not review the problems of plan implementation in Asian centrally planned economies, in Cuba or in Yugoslavia, because developments in these countries have differed considerably from those in the countries of eastern Europe.

main political and social factors influencing methods of planning in the centrally planned economies were state ownership of most of the means of production and the commitment of their Governments to the creation of a communist society.

The nationalization of industry opened the way to direct management of enterprises by the state administration, and naturally led to the creation of a system of plan implementation by means of administrative directives. The impact of these institutional arrangements on methods of plan preparation was no less significant. It enabled the centrally planned economies to create a complex and hierarchical system of planning, organized along the lines of the administrative subdivisions of the economic authorities, from the central planning agency, through the economic ministries, all the way down to individual enterprises. The large number of specific targets included in the central plan were handed down through a process of successive disaggregation to the lower units in the form of obligatory directives covering all aspects of the economic activities of individual productive units and their interrelations. The existence of this system also enabled the authorities to involve all operating units in the process of preparing the national plans. Although some form of participation by producers in the planning process is possible in other economic systems, there is little doubt that its initiation in the centrally planned economies was dictated by the need to verify the feasibility of specific directives.

As stated above, the ultimate goal of development policy in the centrally planned economies is the creation of a communist economic and social order. Since economic planning is regarded as a means whereby this economic and social transformation may be brought about, the impact of this goal on policies of implementation has been quite considerable. While the translation of this concept into policy measures has varied over time, it has, according to some interpretations, implied the retention of state ownership and the extension of its scope, a gradual increase in the share in total consumption of "social consumption", that is, goods and services provided to the consumers free of charge, restraints imposed on differentiation of income and, in the earlier period of planning at least, the gradual elimination of market relations.

The methods of planning and implementation of plans developed in the centrally planned economies and retained until recently with only a few changes were broadly adapted to the economic tasks and political and social conditions prevailing at their inception. There is little doubt, however, that they were not the only possible methods of planning in a socialist economy. It is now widely believed that the recent reforms were long overdue and that even in the earlier stages of planning, more flexible methods might have yielded better results.

While this is undoubtedly the case, it becomes clear, if the problem is viewed in the proper historical perspective, that the builders of the first planning system could hardly be expected to envisage such alternatives. The inability of the market economies to deal with the stagnation and decline of economic activities in the interwar period reinforced the tendency—inherent in the system of state ownership—to rely primarily on administrative methods of management of the economy. Views regarding methods of plan implementation in other eastern European countries which introduced development planning at the end of the Second World War were strongly influenced not only by their own negative experience with market economy but also by the extremely rapid development of the Soviet economy under the system of administrative plan implementation. It was not until post-war experience demonstrated that a market economy need not lead to disastrous economic fluctuations and is capable of expanding at relatively high rates[2] that the idea of a system of "socialist market relations", guided by indirect methods of government intervention, could gain favour in the centrally planned economies.

[2] It is now commonly held that this change was the effect of the expansion of state ownership of productive facilities in the market economies and by the considerable increase in the share of government expenditure in total national expenditure. These new conditions have opened to the Governments the possibility of applying policies which reduce significantly the scope of economic fluctuations generated by the free play of market forces.

Chapter V

GENERAL CONDITIONS FOR THE EFFECTIVE IMPLEMENTATION OF PLANS

Contents of plans and implementation policies

Methods of planning and policies of implementation in the centrally planned economies have undergone considerable changes between the first attempt at development planning in the Soviet Union in the early 1920's and the recent significant reforms of the 1960's.

The most characteristic feature of planning in these countries was the fact that, regardless of differences in scope and in methods of managing the economy, the content of the plans was always directly linked with the possibility of, and the methods used for, their implementation.

In fact, historically, the planning process in these countries grew out of government action in the economic field, which from the outset was considered one of the main, if not the main, obligation of the public authorities. The precedence taken by action in the form of government intervention in economic processes has not resulted in any downgrading of planning. This is clearly demonstrated by the elaboration by these countries of the most comprehensive and intricate development plans. It has, however, prevented that dissociation of planning from implementation policy, which is apparent in several countries where targets are formulated without due regard to their feasibility and are not supported by the decisions needed for their implementation. A no less important consequence of this attitude has been the firm conviction that the application of active development policy need not be postponed until adequate data are available for drawing up all-embracing and fully elaborated plans.

In the early stages of development in the Soviet Union, vigorous action by the Government, concentrated on specific strategically chosen tasks, had a considerable indirect effect on the whole economy. The lack of statistical data, shortage of qualified personnel, organizational shortcomings and the general state of the economy made it impossible at that stage to set up a comprehensive plan which could be implemented. In consequence, economic policy was largely directed by operational programmes devised for the solution of specific problems. It is true that many of these programmes were dealing with current emergencies rather than with development objectives. Other operational programmes, however, aimed at concentrating effort on specific tasks regarded as essential for the growth of the economy at the time in question. Intensive effort aimed at the implementation of basic though limited objectives was considered more important than the preparation of very comprehensive plans for which means of implementation were lacking.

The view that extensive government intervention in, and control of, economic processes is essential to guide the economy along socially desirable paths permeated government policy in the centrally planned economies at all stages of their development. The scope of the plans, the numbers of specific targets, the degree of their disaggregation, their character as guidelines—orientational indicators, obligatory commitments for the central authorities, or directives to the operational units at various levels—varied over time. But in all cases, even when the obligatory targets were limited to specific sectors or branches, their choice was largely determined by their impact on the development of the economy as a whole rather than by the individual profitability of specific undertakings.

Thus, for instance, the first long-term plan set up in the Soviet Union in 1920 was originally limited to the development of electric power over a ten to fifteen-year period. But even this plan was not treated in isolation from the general problem of economic growth and it was from the beginning regarded as a focal point around which other targets were to be elaborated: first, targets for the production of goods required for the expansion of the power network, and then a more integrated plan for the economy as a whole. For the reasons stated above, the attempt to set up an integrated plan for the whole economy proved unsuccessful, however. The first comprehensive medium-term plan was not set up until 1928.

Similarly, the reconstruction plans of the other centrally planned economies, initiated after the Second World War, were not nearly as comprehensive as the Soviet five-year plans or their own plans during the post-reconstruction period. In the following stage, these countries' plans contained a large number of targets covering, in addition to the state sector, the co-operative and private sector which, in the initial period of long-term planning, was quite considerable, especially in agriculture. Even during the period of very extensive and detailed planning, however, medium-term plans were occasionally discarded before their completion, owing to unpredictable circumstances or to their internal defects. In some cases, the discarded plans could not immediately be replaced by new, fully integrated plans. This did not, however, result in any weakening of active development policies, which were in the interim guided by specific programmes.

It is of interest to note in this context that the formulation of all-embracing plans, regardless of the ability or will to implement them, has always been considered in these countries as a pointless and misleading exercise. However, the lack of immediately accessible means of implementing comprehensive plans has never been regarded as sufficient reason to accept more narrowly based plans permanently. Instead, efforts have been directed towards attaining the conditions necessary for the implementation of policies covering all sectors of the economy.

These views concerning the comprehensive nature of planning and the role of government intervention have not been basically altered by the new approaches to planning. The consequence of these new approaches, however, as regards various aspects of planning and above all implementation policies, is most significant.

The most important feature of the economic reforms taking place in the centrally planned economies consists in the enlargement of the scope of the autonomous activities of state enterprises, together with a reduction in the numbers of directive targets. In some countries, these reforms provide for a virtual elimination of the system of implementation of planning through administrative directives. From the point of view of plan implementation, this change places the productive units of the centrally planned economies in conditions similar in some respects to those existing in private enterprise economies. Since the formulation of plans in the centrally planned economies is closely related to the methods and possibilities of implementing various targets, the introduction of new methods of implementation will have a significant impact on the content of the national plans, the number and nature of the targets, and the degree of their aggregation.

The transition to the new system has raised several questions of development planning which have acquired new dimensions in the context of the economic reforms. The most important of these, also relevant to planning in countries with different economic and social systems, are the following:

Should the national plan contain targets which cannot be directly implemented by government order or by budgetary financing? What should be the scope of government intervention? Should the Government be confined to the application of global policy measures, or should it tend to influence the pattern of economic growth by selective policies, applied in a differentiated way to various areas of economic activity?

In view of the importance of these questions, it is of interest to discuss briefly the new approaches to these problems which have emerged from the reappraisal of old policies in the centrally planned economies.

According to present thinking, the introduction of development planning implies recognition of the fact that the spontaneous operation of market forces is not capable of bringing about the desired acceleration of economic growth and achieving the necessary structural changes. In consequence, in the initial stages of industrialization in particular, vigorous government intervention is necessary. In order to be effective, this intervention should not be limited to the sectors directly subordinate to the central authorities but should tend to influence all sectors of the economy. It is also believed that since the required structural changes cannot be brought about by the free play of market forces, government policy cannot be effective if it is limited to global measures in circumstances in which changes in the structure of the economy are of paramount importance. In order to achieve the desired results, Governments are bound to have recourse to selective measures involving preferential treatment of certain sectors or industries. Since the main function of the national plan is, according to those views, to integrate development policies into a coherent system, the scope of the plan should be as broad as the area of government intervention.

In contrast to the views expressed in the past, it is now believed that ways and means of government intervention which have long been considered as inherent in the socialist system should vary in accordance with changing general conditions, and that consequently the nature of the targets included in the plan should also vary.

This attitude does not imply an outright rejection of the methods of implementation by administrative order prevailing in the past. It is in fact noted that, in spite of their shortcomings, the use of these very rigid methods has made it possible to raise the rate of accumulation considerably, to bring about fundamental structural changes within a short space of time, and to accelerate the rate of growth. Such changes could not have been achieved in the circumstances prevailing without reducing the role of the profitability of individual enterprises as the determinant of their activities, and consequently without reducing the part played by market forces in their interrelations. This is particularly true of the less industrialized centrally planned economies.

These considerations are obviously not aimed at justifying fully the former methods and policies of plan implementation. As already mentioned, it is now almost universally agreed that even in the earlier period a greater use of market relations and profitability criteria would have been beneficial. The point which is stressed is that the need for far-reaching structural changes at lower levels of development requires much more stringent government control and regulation than are necessary at higher levels of industrialization. It was the attainment of a higher level of industrialization and the resulting need to adjust the methods of planning and implementation to the new conditions that were the main argument in favour of the present economic reforms.

It is widely agreed that basic structural changes which could not have been achieved without stringent government control did take place in the process of rapid industrialization. The new conditions which emerged from this process call for a change in development strategy. In the past, the development policy of the centrally planned economies was concentrated on the preferential expansion of strategically crucial economic sectors and industries, primarily heavy industries. This was largely achieved through the creation of entirely new industrial branches, the construction of new facilities and the shift of labour to first-priority sectors.

One of the consequences of this strategy, aimed at the creation of new dynamic structures and the maximum integration of material and human resources into productive processes, was that profitability of individual enterprises and the rate of growth of personal consumption had to be subordinated to the main strategic objectives. The structural changes considered desirable from the point of view of long-term development were in the prevailing conditions contrary to the natural tendencies of the market mechanism.

This policy of disregarding the profitability of individual enterprises and limiting the role of market forces was able to yield significant results as long as the growth of the economy could be achieved by a continuous absorption of unused and easily accessible resources and by imposing considerable restrictions on the growth of personal consumption.

One of the consequences of the process of rapid industrialization and the related structural changes, however, was that as the main objectives of that strategy were reached, the conditions necessary for its continuation were disappearing. The gradual exhaustion of the unused resources on the one hand, and the growing need to devote more resources to consumption on the other, led inevitably to a shift in emphasis from the "extensive" to the "intensive" pattern of growth, by increasing the over-all efficiency of economic activities. In more concrete terms, this meant the creation of conditions for raising the profitability of individual enterprises, for a greater adaptation of production to the pattern of demand, and therefore for greater flexibility of all producing units. It is generally agreed that these changes imply a considerable increase in the role of the market mechanism and a substantial reduction in the scope of direct controls, many of which have—at the present stage of development—lost their usefulness and become obstacles to further economic growth.

The enlargement of the role of the market mechanism is not tantamount to a downgrading of the role of central planning and of government intervention in economic processes. It does, however, involve significant changes in the methods of this intervention. The aim of these changes is to reduce considerably the interference of government authorities in the daily activities of enterprises or their associations. Instead, the Government will tend increasingly to induce enterprises to act in conformity with the general objectives of the plan by fiscal, financial and price policies whose purpose is to create conditions which would bring the interests of individual enterprises into conformity with the social goals reflected in the plan. It is believed that this can be achieved if policy measures are differentiated with the view of acting as incentives or disincentives for various sectors or industries. At the present stage, considerable differences exist in the attitude of various countries towards the respective role of directives and indirect means of plan implementation. It is noteworthy that differences concerning the scope left for the application of directives and the degree of differentiation required in the application of indirect measures of implementation depend to a large extent on the importance attached by the various countries to further fundamental structural changes at the present stage of their development.[1]

It will be remembered that even under the highly centralized system, the activities of enterprises could not be guided solely by the directives of the supervising authorities. Although almost all activities of enterprises were subject to directives, the imple-

[1] The expression "fundamental" refers to such changes as the rapid rise of the share of industry in national product, or, within the industrial sector, a shift towards heavy industries and within this group, for example, to engineering. Changes in the share of individual branches or sub-branches within a given industry are not considered as fundamental in the above sense and according to the views expressed in many eastern European countries could be efficiently achieved by the free decisions of producing units aiming at a better adaptation of their output to the market demand.

mentation of the obligatory targets had to be supported by a system of rewards and penalties. While these rewards and penalties were in the past tied solely to the fulfilment of production and other targets, the incentives provided by the new system are increasingly dependent on profitability. In countries which have retained certain important elements of directive planning, the proportion of profits used for rewards depends on the fulfilment of specific planned targets. But in the case of virtual elimination of the system of plan implementation by administrative directives, the rewards are based entirely on the profitability of the enterprises, which in the new conditions will depend largely on their ability to adapt their output to the market demand and to reduce costs. The granting of wide autonomy to state enterprises should not be equated with a complete elimination of all forms of control over their activities. It is in fact believed that the use of indirect methods of implementation and the formulation of specific or general policy measures can be effective only if the planning authorities are able to anticipate the response of the operating units. This forecasting will be greatly facilitated by the existence of a system of rules and regulations providing a unified framework within which enterprises may freely exercise their decision-making prerogatives. These rules define certain rights and obligations of the operating units concerning for example the creation of various funds within the enterprises, the utilization of their net proceeds for various types of rewards, penalties for the violation of freely concluded contracts and agreements etc. The introduction of such rules and regulations is clearly made possible by the fact that in spite of the large degree of autonomy, the enterprises remain State-owned undertakings. It should be added, however, that the impact of many of these regulations on decision making by enterprises is not very different from that of certain legal and statutory arrangements in the private enterprise economies.

These changes in methods of implementation have a significant impact on the content of plans and on the character of the planned targets. Even under the old system of planning, not all the targets of the national plan were identical in character. Some of them represented firm decisions which were by a process of successive disaggregation translated into operational directives handed over to all agencies and enterprises. Other targets were presented in the form of "limits" which could not be exceeded without the express permission of the higher authorities. Still others were never transformed into directives of any kind to the lower units. Thus, for instance, in recent times, the collective farms received no directives concerning the volume and composition of their output, although they were obliged to sell to the state purchasing agencies specified amounts of various commodities, the aggregate volume of which was indicated in the national plan. The national plan also contained, however, in addition to the delivery quotas, targets for the growth of agricultural production and of the national product, of which it is a component. The character of this target was clearly different from that of the targets set for the industrial production of state enterprises.

The introduction of the new system of plan implementation leads first of all to a reduction in the number of detailed targets contained in the central plan. This reduction is directly related to the narrowing of the scope of directive planning. It is obvious that those targets which are not to be translated into specific directives can be presented in the national plan in a more aggregated form than in the past. Moreover, some of the targets included in the old plans may not be included in future, even in aggregated form, in cases where no special policy measures are required to obtain specific results, either because these results have no bearing on the achievement of general goals or because they are indirectly influenced by policies affecting the implementation of other targets. In countries where the directive method of plan implementation has been or is to be almost entirely abandoned, many of the former obligatory targets are taking the form of orientational indicators which are regarded as guidelines for government policy rather than unqualified commitments.

It is noteworthy that the narrowing of the area of economic activity subject to direct administrative control and the change in the number and character of the targets contained in the national plans do not reduce the comprehensiveness of the plans, which will as before encompass all the main fields of economic activity. No less important is the fact that even in countries where the targets included in the national plan will not be translated into directives, the most important of these will retain the character of obligatory commitments, as far as the central authorities are concerned, to which the economic policy of the Government must be subordinated.

Since the purpose of the new system is to create the widest possible opportunities for the exercise of initiative by the management of individual enterprises, the general tendency is to limit government intervention to the minimum considered adequate for the fulfilment of development plans. It is generally believed that the rationalization of the price system[2]

[2] The rationalization of the price system consists largely of bringing about a much closer relationship between relative costs and relative prices and of allowing for relative scarcities in fixing prices of producer goods which, unlike

should considerably reduce the need for specific policies concerning the current activities of enterprises which are largely predetermined by the existing economic structure. Since, in the short run, the main objective of the reforms is to improve co-ordination and raise the profitability of existing enterprises, it is felt that this can best be achieved by the market mechanism, regulated by fiscal, financial and price policies.

A much greater degree of government intervention is considered to be necessary in fields of activity which impinge upon long-term economic and social problems. Thus, problems related to the determination of the rate of growth, the rate of accumulation and the desirable composition of output, as well as to the distribution of income and the pattern of future consumption, cannot, according to the prevailing views, be rationally solved by the free play of market forces.[3]

In consequence, in most of the centrally planned economies, the planned allocation of investment by economic sectors or individual branches continues to be regarded as one of the most essential commitments of the central authorities. The need for such commitments is, however, considerably de-emphasized by the most industrialized countries in the group.

The implementation of investment plans is to be carried out increasingly by means of credit policies, while the proportion of investment directly financed by budgetary means is to be substantially reduced. The granting of credits to individual enterprises or associations within branches will be determined not by government order but by the decision of the banks, on the basis of their evaluation of the profitability of various undertakings. In most countries, however, the branch allocation among branches of the major proportion of investment credits will be determined by the credit plan formulated in conformity with the pattern of allocation of total investment under the national economic plan.

Methods of implementation of investment targets will not be confined to budgetary and credit policies. An increasing proportion of investment will be financed out of profits left at the disposal of the enterprises or their associations. Taxation and price policies affecting the net profitability of various branches and enterprises will also play an important part by encouraging investment in some sectors and discouraging it in others, in cases where a system of priorities is laid down in the plan.

It has been pointed out that some of the policies for the implementation of investment plans gradually being introduced in the eastern European countries do not differ basically from those which might be applied under the system of private enterprise in countries planning for structural changes and the acceleration of economic growth. Some of the methods of government control, such as building permits, customs privileges for specific investment goods, and even selective credit policy, have in fact been applied in some of these countries at certain periods. It is clear, however, that where the State owns most of the means of production, the possibilities of influencing the pattern of economic growth are much greater than in private enterprise economies, even when Governments are determined to reduce or eliminate altogether methods of direct intervention in and control over state enterprises. Two points have been brought out in this connexion. One, that state ownership reduces considerably the possibility of the emergence of strong pressure groups representing the interests of specific sectors or industries which may prevent Governments from applying selective policies. The other, that the managers of state enterprises are responsible to the state authorities and can therefore be dismissed not only if they violate the rules and regulations relating to the activities of the enterprise in question but also if they disregard the long-term interest of their enterprise in favour of current gains.[4]

---

those of consumer goods, used not to be influenced by this factor. The general tendency is to reduce the number of commodities the prices of which are centrally determined and to apply general price controls over large groups of commodities rather than to fix the prices of each commodity within the group.

[3] It has been argued that although the composition of a certain proportion of consumption may be unimportant from the point of view of economic and social progress, this is not true of total consumption. Thus, for instance, the choice between the alternative expansion of the supply of passenger cars for individual consumers or that of buses and other State-owned means of public transport, should, according to some views, be decided in the process of the preparation of long-term and medium-term plans, on the basis of such considerations as the degree of traffic density in the cities, the desirability of channelling resources into housing rather than individual motor vehicles, the socially desirable distribution of incomes and its effect on the pattern of demand, and so on.

[4] This problem has been raised in western as well as eastern European literature in connexion with the new economic reforms. It has been argued that while the new system linking rewards to profits may induce managers to maximize the short-run efficiency of enterprises, the dissociation between ownership and management will tend to induce the manager to disregard the long-term interest of the enterprise in favour of current profits. According to these views, the manager of a privately owned enterprise is concerned about its future either because of his ownership and inheritance rights or, in the case of corporations, because of the effect of future prospects on the value of the stock. A decline in stock prices directly affects the welfare of the managers who own a certain proportion of the stock, and may also lead to their dismissal by decision of the stockholders. In such circumstances, management is vitally interested in the future of enterprises and is not inclined to sacrifice the long-term interest to current gains. The conclusion drawn implicitly or explicitly from this has been that autonomy of enterprises without the restoration of private ownership cannot be effective. These views have been strongly disputed on the following grounds: first, that

(foot-note 4 continued on page 90)

Moreover, although the purpose of the reforms is to create conditions in which the self-interest of enterprises will induce them to conduct their current activities and to initiate investment programmes in conformity with the medium-term objectives, even the most advanced reforms do not reject the possibility of using directives if and when indirect methods of implementation fail. This is not to say that the Governments of these countries intend to apply administrative methods in all cases in which actual changes depart from the planned ones. Already the fact that the targets included in the national plan are to be presented in a more aggregated form than in the past clearly indicates that the composition of certain aggregates is not considered to be of primary concern for the achievement of the plan's general objectives. What is more important is that many targets are not to be regarded as immutable but are to be subject to change in the light of experience. In consequence, the reinstatement of the abandoned directives will be called for only in cases where deviations from the planned targets risk diverting available resources from the activities regarded as essential for the achievement of the optimum rate of growth and needed structural changes.

This attitude towards the eventual reinstatement of some of the discarded directives clearly indicates that the increased flexibility of planning and implementation does not imply any reduction of government responsibility for the fulfilment of the main objectives of the plan. It is in fact believed that even a partial replacement of the firm and detailed targets by more tentatively formulated objectives would not be justified if the commitment of the Government to an active development policy was less firmly established. Similar opinions have been expressed with respect to implementation policies. According to these views, the general attitude of the community and of the public authorities towards the role of government intervention in economic processes has a considerable bearing on the need for including in the national plan clearly defined implementation measures and policies. The inclusion of such measures is believed to be much more important in cases in which the text of the plan is the sole document committing the Government to the pursuit of development policies than in countries where active development policy is a normal and obligatory function of the central Government.

Under the old system of planning and management, when almost all aspects of the activities of enterprises were subject to directives—regulating inputs, outputs, delivery of goods, remuneration of labour and management, cost, profits etc.—special implementation policies played a subordinate role. Under the new conditions, the formulation of implementation policies during the process of preparing national plans becomes much more important. This is particularly true of the price, credit, fiscal and financial policies which are reflected in the financial plans. But even in these conditions, the need for a precise definition of these measures in the medium-term plan is not of primary importance, because of the total commitment of the Government to the implementation of the plan, regardless of whether it does or does not contain specific implementation measures.

In view of this, the main reason for formulating implementation policies, and rules and regulations governing the activities of producing units for a prolonged period, is to enable these units to prepare their own programmes of action on the basis of relatively stable policy parameters. It is noteworthy that the policy measures elaborated in medium-term plans are to be rather global in character, that is, uniformly applied to all enterprises within a branch, or in some cases to several or all branches within a given sector. In the context of annual plans, these measures will be supplemented wherever necessary by other more diversified and specific measures, in order to deal effectively with current operational problems of plan implementation.

The foregoing review has indicated the general trend of the changes that have taken and are taking place in methods of planning and plan implementation in the eastern European centrally planned economies. The actual changes made thus far in these methods vary from country to country. While the number of directives handed down to enterprises has been considerably reduced, in most of these countries enterprises are still subject to directives regarding investment, the volume and the composition of output (expressed in terms of sales), the wages bill and profits. The system of allocating basic raw materials and intermediate goods as well as machinery and equipment has also been temporarily retained, although an increasing proportion of transactions is to be conducted on the basis of freely concluded agreements between various enterprises. Obligations concerning the composition of output are being gradually reduced and profitability is becoming the main criterion of success on which the rewards paid out from the enterprise's profits will depend. The share of the profits left at the disposal of enterprises is being considerably increased, and their right to use their own funds, supplemented by bank credits,

(foot-note 4 continued from page 89)
the assertions concerning the relationship between the long-term prospects of enterprises and the movement of stock prices as well as the effect of such movements on managerial behaviour are not substantiated by empirical evidence. Secondly, that the prospective reduction of rewards as well as the fear of dismissal by the state authorities is a far more effective means of influencing the activities of management than highly hypothetical decisions by stockholders' meetings.

for freely determined investment is being expanded. Budgetary grants for centrally determined investments are being replaced by interest-bearing and repayable loans.

Notwithstanding differences in the timing of the reforms and the amount of decentralization already achieved, there is little doubt that all the eastern European countries are moving towards the elimination of directives as the main instrument of plan implementation. Thus far, only Czechoslovakia has virtually abolished the use of directives in the implementation of plans, and Hungary has announced similar changes for 1968.

The timing of these reforms and their scope were obviously influenced by a variety of economic as well as political factors. Among the purely economic considerations, the one most often singled out has been the level of industrialization reached by individual countries and the importance attached to fundamental structural changes. These considerations have influenced not only the role of directives in plan implementation but also decisions concerning the relative importance of global and specific policies in various fields. Thus, for example, although both Czechoslovakia and Hungary have decided to abandon the use of directives as a means of plan implementation almost entirely, the attitude of these countries with respect to the allocation of investment differs substantially.

In Hungary, the national plan is to contain both the total volume of investment and its allocation by sectors and branches in the form of obligatory targets to be implemented by selective credit and other policies. In contrast, the Czechoslovak plan contains no firm commitments concerning the allocation of investment by branches or sectors. This innovation, unprecedented in any centrally planned economy save Yugoslavia, is clearly related to the fact that, according to widely held views, at the present stage of Czechoslovakia's development the principal need is to secure improved adaptation of production to current demand and higher efficiency of producing units rather than to bring about major structural changes. In view of this, there is less need for central allocation of investment,[5] the major part of which can, in the present circumstances, be more efficiently distributed by the banking system in response to the demand of enterprises and on the basis of an evaluation of their productivity. The example of Czechoslovakia offers the best illustration of the problems involved in the transition to the new system of planning, both because the reforms achieved by this country are by far the most advanced and because they were formalized in an operational decree of the Government and put into effect as of 1 January 1967.[6]

THE NEW METHODS OF PLAN IMPLEMENTATION IN CZECHOSLOVAKIA

One of the most important changes reflected in that document is the significant differentiation of the character of the targets included in the plan. Although the new plans will continue to be very comprehensive and to contain targets covering all major aspects of economic activities, not all of these targets will be equally binding.

First in importance will be the general concept of development outlined for the period covered by the medium-term plan, and the over-all objectives expressed in the form of quantitative targets for broad aggregates such as national income, consumption and accumulation, and reflected in other global aims of major importance. These targets and goals are conceived as the basic commitments of the central authorities to which all policy measures should be subordinated.

In addition to these general objectives, the plan will also contain more specific targets, the implementation of which is considered not as a goal in itself but rather as a means of achieving the main objectives. Most of these targets are defined as "orientation targets", and concern various aspects of economic activity, which in the former system were considered to be compulsory and were translated into obligatory directives for ministries, other intermediate agencies and individual enterprises. One of the most significant features of the new system is that these targets have lost their obligatory character not only for the operating units but also for the central authorities which are now fully committed only to the achievement of the main objectives outlined above.

The main function of the orientation targets is to provide the executive agencies and productive units and organizations with specific guidelines indicating the pattern of changes which appears to be most desirable for the achievement of the major goals and objectives of the plan. These targets are elaborated in conjunction with the formulation of the general obligatory targets, through a process of successive approximations during which all the targets are mutually adjusted and their feasibility tested by the use of commodity and other balances so as to arrive at an internally consistent and realistic national plan.

It is important to stress that while the orientation targets contained in the central plan may be handed over to the operating units in a disaggregated form,

[5] With the exception of a certain number of projects of major importance.

[6] See "Czechoslovak Government Order No. 100 of 12 December 1966", *Sbirka Zakonu Ceskoslovenske socialisticke republiky,* vol. 1966, No. 44 (Prague, 20 December 1966).

their main function remains that of notifying the enterprises or their associations of the desirable pattern of their output, leaving them entirely free to conduct their business along the lines dictated by their own interest. The role of these targets may be described as similar in a certain sense to the role which, in countries with a different economic and social system, might be played by the information provided by the central planning agency to the operating units, concerning the prospective demand for their goods and the supply of various inputs required for their production.

While most of the former directive targets have been replaced by orientation targets, some of the specific tasks of the plan have retained a compulsory character, both for the central authorities and for the agencies or enterprises to which they are to be passed on in a disaggregated form as directives. The relatively narrow scope of these targets, defined in the government decree concerning the new system as "firm targets" or "firm limits", is clearly apparent from the following enumeration of such targets incorporated into the 1967 plan. Firm targets are set in this plan for (*a*) basic research in applied science and geological prospecting; (*b*) a limited number of selected investment projects; (*c*) the prime objective of growth in the less developed regions; (*d*) targets relating to national defence security.[7] The most important firm limits define the total volume of fixed investment (not broken down by sectors or branches) and the subsidies to be paid to individual branches by the state budget during the period covered by the plan.

The decision to reduce sharply the number for firm targets and limits included in the national plan does not deprive the Government of the right to increase the number of such targets if necessary. The decree of the Czechoslovak Government concerning the new system stipulates explicitly that the number of such targets included in the national plans and translated into specific directives to lower executive bodies and producing units may be increased, if the general objectives of the plan cannot —under given circumstances—be achieved otherwise.

In such cases, the plan may include the following additional firm targets and limits: targets for the output of a limited number of specific commodities expressed in physical units, as well as for the allocation of specific commodities by main customers,[8] and certain targets concerning the training and recruitment of labour, including the distribution of high-school and college graduates among various professions. Moreover, specific measures will be introduced on a temporary basis in the field of foreign trade either in the form of firm targets and limits for exports and imports or in the form of a net balance of foreign transactions set for various enterprises or their associations.

The number of firm targets and limits contained in the original version of the plan can be increased in the course of its implementation if deviations from the orientation targets risk endangering its general objectives. Thus, according to the government decree on the new system of planning:

> "The organs of economic management analyse the deviations of actual economic developments from the orientation targets and on this basis take the necessary decisions concerning the use of operational economic instruments and the required measures concerning reserves, imports, investment etc. If the deviations of actual developments from the proportions set in the state plan and expressed in the orientation targets are likely to endanger substantially the implementation of key goals of the state plan and the state budget, the Government will set additional obligatory limits or instruct the central agencies (or regional national committees) to maintain the basic proportions established by the plan and the budget by the establishment of extraordinary firm targets in all instances when the use of economic instruments would prove to be ineffective."[9]

It is noteworthy that, according to this decree, recourse is to be had to the use of additional directives in the process of implementing the plan only as a last resort after efforts to secure the necessary corrections by the use of economic instruments have failed.

The main economic instruments of plan implementation listed in the government decree are of two types: "long-term economic instruments" and "operational economic instruments". The long-term economic instruments are as a rule to be applied uniformly in all areas of economic activity and are to be fixed for the entire period covered by the medium-term plan. In contrast, the "operational economic instruments", as indicated by their name, are to be used in response to changing circumstances and, no less important, are to be applied in a differentiated way in accordance with the specific aims of government policy in various sectors and industries.

The long-term economic instruments consist of a system of levies designed to influence the operations

[7] The projects included in the national plan in the form of firm targets will relate mainly to non-productive investment, fuel and power, productive facilities of particular importance for exports and investment of special importance for the application of the most advanced achievements of scientific research.

[8] It is noteworthy that, according to the prevailing opinion, the introduction of such additional firm targets is likely to be required only during the first transitional years of operation of the new system. The plan for 1967 includes such targets for twelve commodities only.

[9] Source quoted in foot-note 6.

of enterprises in certain ways. Thus the levies are intended, *inter alia,* to induce enterprises to increase their efficiency, to regulate the amounts of the net proceeds or profits left at their disposal, and to influence the disposition of their revenues in conformity with the general interests of the economy. It should be noted that the rates of the various levies are established prior to the preparation of the preliminary draft of the plan[10] and are communicated to the enterprises in order to enable them to prepare their work programmes with full knowledge of the impact of these levies on their finances. This procedure is motivated by the fact that the final version of the national plan has to take into account the programmes of the enterprises which, under the new system, are formulated by them in conformity with their own interests.

Among the five long-term economic instruments listed in the decree of the Czechoslovak Government, the "levy on gross income or profit" is intended to control the funds left at the disposal of enterprises for wages, investment and other outlays.[11]

The "levy on fixed assets" is designed to induce enterprises to improve the degree of utilization of their existing capacities and to economize on further extensions. The fixing of the rate of this levy, which is bound to influence the demand for investment, will be an important instrument for keeping the autonomous investment activities of enterprises in line with the total volume of investment stipulated in the national plan.

The long-term economic instruments include also a "levy on inventories" and a "stabilization levy".[12] The first is to restrain the excessive growth of inventories, which in recent years caused considerable losses to the Czechoslovak economy. The stabilization levy is assessed on the increment of the wage bill, and its purpose is to control the inflationary effects of an excessive increase in incomes per worker as well as to discourage an excessive rise in employment. The importance of the last-mentioned factor is due to the shortage of labour which has been apparent in Czechoslovakia during recent years. It should be added that in contrast to the other long-term instruments, the stabilization levy may be used in a differentiated form so as to encourage or discourage the movement of labour to and from various regions or even specific economic sectors.

As noted previously, these long-term economic instruments are supplemented by operational instruments, much more numerous and designed to be used in the process of implementing the medium-term plan as additional means of implementing its annual segments or as corrective measures in cases in which deviations from the orientation targets risk preventing the fulfilment of the basic objectives of the national plan. Accordingly, unlike most of the long-term instruments, the operational instruments need not be applied uniformly to all sectors, branches or commodities. The type of measure used, the area to be covered and the extent and direction of the changes to be brought about by the application of these measures will vary according to circumstances.

Among the operational economic instruments listed in the government decree, the most important relate to (*a*) price and wage policies; (*b*) additional loans and fines as well as subsidies and tax relief measures for specific enterprises or their associations; (*c*) credit and interest rate policies; (*d*) rules and regulations dealing with the obligatory allocation of net revenue of enterprises among various enterprise funds, such as wage, investment and reserve funds. While the operational economic instruments are to be applied in various fields of economic activity, the government decrees indicate separately two areas in which these policies are explicitly linked with the achievement of specific objectives. They are to be used extensively to induce a rise in the efficiency of foreign trade and to encourage faster than average growth in the less developed regions.

Although the general guidelines concerning credit, interest rate and price and wage policies are formulated in the context of the medium-term plan, their application during each year of the plan will obviously have to be adapted to the short-run changes.[13] The changes in the levels of prices in individual branches over the medium-term period are to be indicated in a special "plan of development of price levels" and if the objectives of that plan cannot be achieved by other means, the price levels of industries, branches or even of major groups of commodities may be fixed by the central authorities.[14]

[10] This is also true with respect to the general guidelines concerning credit, interest rate and price and wage policies for the medium-term plan.

[11] The concept of "gross income" introduced in conjunction with the new reforms can be defined as total proceeds less cost of materials, intermediate goods and depreciation. Its introduction has been closely related to the elimination of directives covering the wages and investment funds of enterprises which, under the new system, depend on those enterprises' autonomous decisions concerning the allocation of the "net income" left at their disposal after the deduction from their gross income of various levies and other financial obligations.

[12] There is also a levy on depreciation which is conceived of merely as a temporary device for equalizing differences between the financial circumstances of various enterprises arising out of the fact that, in the past, capital assets were granted free of charge to enterprises by the state budget, while they are now financed by interest-bearing, repayable loans.

[13] The measures to be introduced in the course of the year are to be announced before the final formulation of the annual plan.

[14] "The movement of price levels in industries, branches and even in major groups of commodities is defined by the plan of development of price levels—formulated in accordance with the objectives and conditions of the future development of the national economy—which provides the basis for the price policy of the central Government. If the

(foot-note 14 continued on page 94)

This statement seems to imply that the central authorities intend to influence the price movements by indirect means affecting demand and supply, and resort to direct price controls only if the other means fail to keep the levels of prices in line with the price plan.[15] Although the enumeration of the operational economic instruments and the fact that they can be applied in a discriminatory way provide a clear indication of their role as instruments of plan implementation, it would be pertinent to close this description by stressing the following points of special interest.

The first is that the operational economic instruments are to be used only in special circumstances, and that the general policy of the Government is to avoid undue interference with the play of market forces.

The second point is that the main purpose of these instruments is to guide the development of market relations along the lines most favourable for the accomplishment of the major objectives of the plan, without interfering directly with the decision making of the state enterprises. Only one of these instruments restrains the freedom of decision of enterprises, by intervening in the allocation of their funds among various uses.

The last point, of more general interest, is that several of these measures are in many respects similar to certain fiscal and financial policies used in private enterprise economies to control inflationary or deflationary tendencies. Furthermore, a differentiated application of indirect tax rates, price support and tax relief policies or of customs duties and import licensing is a common practice in countries with various economic and social systems. In Czechoslovakia their purpose is not only to avoid current imbalances but, mainly, to facilitate the implementation of development plans.

(foot-note 14 continued from page 93)
objectives of the plan for the development of price levels cannot be achieved by other means, price levels of industries, branches and even of major commodity groups will, to the extent necessary, be determined in obligatory form." (Czechoslovak Government Order No. 100 of 12 December 1966.)

[15] These provisions clearly apply only to commodities not subject to direct price-fixing by the central authorities. At present, prices of a significant number of specific producer and consumer goods are fixed individually by the central authorities. But for some commodity groups only a general price level is indicated for each group as a whole while for certain consumer goods entirely free prices exist.

Chapter VI

FINANCIAL PLANNING

Annual plans, budgets and financial planning

Under the planning system of the centrally planned economies, only the annual plans are fully operational in character. The long-term plans, covering a period of ten to twenty years, represent as a rule a broad conceptual framework, indicating the desirable pattern of economic development and the broad outlines of the needed long-term structural changes, within which the medium-term and annual plans can be formulated. In most cases, only a limited number of objectives are quantified in the form of growth indices for a few basic industries. These long-term plans contain no provisions concerning implementation and, in consequence, do not assign any specific tasks to the ministries responsible for the various industrial branches or to producing units. The plans are prepared by the central planning agencies in co-operation with various scientific institutes, but because they are so general in character, operating units do not participate in their formulation. Medium-term plans, on the other hand, present a fully integrated programme containing a large number of quantitative targets covering all aspects of economic activity. The major tasks set out in the medium-term plans are assigned to various executive agencies, and in a more disaggregated form to branch associations and individual enterprises. They may be stated in the form of administrative directives, or they may serve only as orientation targets for the central authorities or for the lower operating units. The major objectives of medium-term plans have the character of commitments, which government policy must respect. Unlike the long-term plans, medium-term plans define the broad policy measures required for their implementation. They are also broken down as a rule into annual segments which serve as a basis for the preparation of operational annual plans.

The fact that annual plans serve to implement medium-term plans and their main objectives are already defined in these plans does not reduce their importance in the planning of economic development. Annual plans have always been regarded as vital to the implementation of long-term and medium-term objectives. In view of their operational character, these plans are as a rule more detailed than medium-term plans, and many of the latter's targets are presented in the annual plans in a more disaggregated form. Much greater participation by the producing units is required in the preparation of the annual plans, to ensure that they are operationally valid. Consequently, communication between the higher and lower echelons, from the central planning agencies and industrial ministries all the way down to the individual enterprises, is even more important in the preparation of annual plans than in the case of medium-term plans.

This method, in which executive agencies and producing units participate widely in the preparation, is considered in the centrally planned economies to be essential for testing the feasibility of the preliminary plan targets, and revising them in the light of the feedback of suggestions from the operating units. Clearly, a realistic formulation of operational plans and policies covering all sectors of the economy and, under the highly centralized system, the formulation of specific directives, was of particular importance in the preparation of annual plans. The verification of the feasibility of the preliminary targets through consultations with various operational units and executive agencies was accompanied by the preparation of a great number of material and other balances, comparing prospective requirements and supplies of real resources with production targets, to ensure that the plans were internally consistent.

The annual plans drawn up in this way frequently differed from the objectives set for a given year in the medium-term plans. This was due largely to the fact that the purpose of the annual plans was to adapt these medium-term objectives to changing short-term conditions and to ensure the short-term equilibrium of the economy.

Accordingly, the formulation of specific policy measures and the drawing up of financial plans and balances played a much greater part in the preparation of the annual than of the medium-term plans.

It is one of the significant features of the centrally planned economies that the main function of the financial plans and balances, including the state budget, is to serve the implementation of development plans. Under the highly centralized system, this was largely achieved by budgetary appropriation and distribution of most of the resources used for investment purposes. Under the new system emerging from the economic reforms, this role of the budget may be substantially reduced, but budgetary policies will be increasingly used as a means of inducing the management of enterprises and their associations to act in conformity with the annual economic plan.

It follows from the above that, unlike countries in which the annual budget is the sole official document reflecting some of the objectives of the medium-term plans, in the centrally planned economies the link between the medium-term plan and the annual budget is established indirectly, through the annual economic plan.[1] It has already been pointed out that the budget is part of a comprehensive system of financial plans, which even before the recent reforms played an important part in the planning process. The importance of financial planning stems from the fact that in the centrally planned economies, as in private enterprise economies, state enterprises, financial institutions, government agencies and households conduct their transactions in monetary terms and are bound as a rule to balance their expenditures with their receipts.

The purpose of the system of financial plans and balances is to determine or to influence the pattern of these monetary flows for each of the above-mentioned sectors, in close co-ordination with the requirements of the national economic plan.

The system of financial planning in use in the centrally planned economies contained a number of accounts and subaccounts similar in many respects to those of national accounting and economic budgeting systems in private enterprise economies. Although there were differences in the form of these balances in the various centrally planned economies, they consisted generally of the following accounts: the state budget, the financial plan of state enterprises, a credit plan, a cash plan, and the balance of money income and outlays of the population. As a group, they reflected the planned financial relations between the budget, state enterprises, other productive sectors, financial institutions and households, and were integrated into a single consolidated "aggregate financial plan of the national economy".[2]

Not all of these plans were equally binding in character. In fact, only the state budget, after approval by the legislature, had the character of a legal commitment. The credit plan and cash plan formed the basis for more detailed instructions handed down to the banking system. The financial plan of state enterprises excluded operational transactions and limited itself to items which together formed a kind of appropriation and capital account. This balance was prepared on the basis of preliminary financial plans supplied by the enterprises which, after final co-ordination with the budget and credit plans, were sent back to the operating agencies and units in a revised form. The "balance of money incomes and outlays of the population", which corresponds roughly to the household sector in other accounting systems, contained no obligatory commitments. Nevertheless, it was closely related to and strongly influenced by the plans concerning retail sales and the wage bill and other income payments.

It was the duty of the planning office and other central agencies to ensure that those plans and balances which were to be translated into specific directives and policy measures were not only mutually consistent but conformed to the targets and priorities laid down in the national economic plan.

The close link between output and other targets of the national economic plan, the budget and other financial plans and balances, made it imperative to associate in its preparation, together with the ministry of finance, the central planning agency, the ministries responsible for individual industrial branches and other executive bodies. Although administrative expediency would demand a clear-cut definition of the responsibilities of each of these bodies at every stage of the planning process, the experience of the centrally planned economies has demonstrated that it is hardly possible to formulate any general criteria for the most efficient distribution of tasks among all these agencies.

While in some countries and at certain periods the establishment of the various financial balances has been the exclusive responsibility of the financial department of the central planning agency, in other countries, or at other times, this function has been vested in the ministry of finance, or, sometimes, made a joint responsibility. Thus, in Poland, the Planning Commission is responsible for the preparation of all financial balances. This is apparently also the case in Eastern Germany. In the USSR, the

[1] This relationship may become more direct under the new system of planning. As will be seen later, the policy parameters established in the context of the medium-term plan will have a direct effect on the annual budget and other annual financial plans.

[2] For a more detailed description of the system of financial plans and balances, see *World Economic Survey, 1960* (United Nations publication, Sales No.: 61.II.C.1), chapter 3.

credit and cash balances are prepared by the Central Bank, while the balance of money incomes and outlays of the population is prepared by the Ministry of Finance in co-operation with the Central Bank. The aggregate financial balance of the state enterprises is prepared by the Ministry of Finance with the help of the industrial ministries and the enterprises subordinate to them. The final co-ordination of the financial plans and balances and their ultimate integration into the aggregate financial balance of the economy is carried out in most countries by the central planning agency in co-operation with the ministry of finance. In Czechoslovakia, the Ministry of Finance was responsible for the preparation of most financial plans and balances and their coordination with the state budget. The preparation of the credit and cash plans as well as the balance of money incomes and outlays of the population, and the final aggregation of these balances into the consolidated financial balance of the national economy was performed by the Ministry of Finance in close co-operation with the central planning agency.[3] It is generally agreed that the pattern of the division of responsibilities among planning or executive agencies is not of prime importance, as long as all these agencies co-operate closely with each other.

It has been seen that one of the most distinctive characteristics of the budget in the centrally planned economies is its full integration into the system of economic and financial planning. The budget is subordinated to the requirements of the national economic plan and is linked at all stages of its preparation with the general planning process. This is done by the ministry of finance, which is under an obligation to work out the budgetary estimates in accordance with the targets in the national economic plan. Since the financial implications of most of the targets are reflected in the financial balances enumerated above, one of the most important functions of the budgetary authorities is to ensure full co-ordination of the various revenue and expenditure items in the budget with those of the other financial balances which, together with the budget, are consolidated in the aggregate financial plan.

The relationship between the various plans and balances may be illustrated by the following somewhat simplified examples. The profit and turnover taxes which are the major sources of budgetary revenue have as their counterpart the corresponding debit items in the financial balance of the state enterprises. Their volume is also closely related to the output and sales targets of the state enterprises indicated in the annual plan. Similarly, the investment expenditure in the state budget, which accounts for most of the investment outlay in the national economy, is closely related to the investment plans of enterprises, and figures on the credit side of the financial balance of the state enterprises.

A somewhat different link exists between the budget and the balance of money incomes and outlays of the population. While this balance is debited with the budgetary revenue from direct taxes, it is credited with budgetary transfers to households in the form of social security payments, pensions and similar income payments. The link between this balance and the national economic plan is obvious if it is remembered that the annual economic plans contain indicators for wages as well as for the retail sales which absorb the major proportion of the money outlays of the population. Administrative expenditure as well as budgetary outlays on "social consumption" are determined in accordance with the corresponding targets in the national economic plan.

It should be emphasized, however, that the strict subordination of the budget to the plan does not necessarily imply that the former is only a passive reflection of the latter. Even under a highly centralized system, the preparation of the budget was supposed to involve consultation among all the agencies concerned. The formulation of financial programmes and of the targets of the national economic plan is conceived as a two-way process, which may lead either to the adaptation of the financial balances to the national economic plan, or to a revision of the targets initially included in the latter.

The process through which these adjustments are arrived at may be summarized as follows. In a first stage, the preliminary targets of the economic plan are compared with the corresponding entries in the financial balances. Then, if any discrepancy is found, attempts are made to introduce changes into the various parameters of the financial plan, or to revise certain of the targets of the economic plan, or both. This process of mutual adjustment continues until a reasonable degree of consistency is achieved.

The process can be illustrated by the methods used for reconciling the balance of money incomes and outlays of the population with the output and income targets of the economic plan and the budget. Thus, for example, if the balance in its preliminary form disclosed discrepancies between prospective demand and supply, it might lead to the revision of the preliminary targets set for production, imports and sales of various commodities. Such a change might affect the budgetary revenue from profits as well as the budgetary expenditure on investments. The read-

[3] See *Ceskoslovenske finance* (Prague, 1958), page 407; *Finanse Polski ludowej w latakh 1944-1960* (Warsaw, 1964), page 126; *Planirovanie narodnogo khozjajstva SSSR* (Moscow, 1965), page 525; *Deutsche Finanzwirtschaft,* No. 16, 1965 (Berlin), page 10.

justment might also be attempted by changes in direct taxes which would influence budgetary reserves directly, or by changes in credit policy affecting the credit plan, or even by modifications of the wage policy outlined in the national economic plan. Alternatively, the readjustment might be brought about by an increase or a reduction of retail prices of various commodities, through modifications of the turnover tax which would be directly reflected in a change in budgetary revenue. Similar problems would arise if the preliminary financial plan for enterprises indicated a discrepancy between the profits left at their disposal and other funds allocated to them for investment and the investment outlays required for the fulfilment of the plan.

In such a case, the required readjustments might be brought about by changes in the profits tax which would affect revenue, or by changes in the budgetary allocation of investment funds to the enterprise sector or by changes in the credit plan. If the attempt to readjust these discrepancies by financial means proves impossible, it serves as an indication that the cause of the imbalances resides in inconsistencies in the economic plan, which will in turn lead to the revision of some of its targets, including, if necessary, the reduction of the originally planned volume of investment.

This process of readjusting financial and economic plans is of course much more complex than would appear from the foregoing description. However, these examples seem sufficiently explicit to indicate the active part played by financial planning in the process of preparing and implementing over-all economic plans.

It will be noted that many of the concepts relating to financial planning and budgetary procedures were developed in conditions in which the management of the economy was highly centralized. In these conditions, financial relations were relatively simple. Most of the resources available for investment were transferred to the budget and then redistributed to enterprises, either directly or through the banking system, for investment purposes. The banking system itself was strictly subordinate to the central authorities. Furthermore, control over monetary and financial flows was greatly facilitated by regulations such as those prohibiting interenterprise loans, requiring enterprises to deposit their liquid assets with the state bank, and prohibiting the use of funds for any purposes other than those specified in the plan. While the use of financial methods was obviously quite important, even under the highly centralized system, it should be remembered that under this system, maintaining over-all economic equilibrium and guiding economic activities in line with the development plan was done largely through a system of direct controls.

There is no doubt that the transformations in systems of planning and management initiated in recent years and now under way in most of the centrally planned economies will have a considerable impact on the techniques used in financial and budgetary planning. The greater autonomy of enterprises and the increase in the share of profits left at their disposal will increase the role of the banking and credit systems in the mobilization of savings. Similarly, the increased role played by private saving in the financing of private housing and other consumer expenditures calls for an expansion of and greater flexibility in financial institutions concerned with this field of activities.[4] The need for innovations in this field may be clearly seen when it is realized that, under the new conditions, individual enterprises may wish to increase their investments over and above the amount of their own liquid assets, while others may wish to postpone the use of their retained profits for investment purposes. Such problems did not exist in the past when most of the profits were paid into the budget and when most investments were financed through budgetary allocations. The needs arising out of these new conditions may lead to increased autonomy for the various banks, to the extent even of their being set up as independent undertakings subject only to general controls similar to those exercised by the State over industrial enterprises. This of course does not rule out their subordination to the regulations of the central bank which, according to circumstances, may be of a general or a selective nature.

These changes in the role of financial institutions and policies should be viewed within the broader context of important modifications in financial planning linked with the present economic reforms. The reduction of the role of directives and, even more, the complete elimination of directives as a means of implementation, considerably increases the role of fiscal and financial policies in the implementation of plans. In these circumstances, budgetary and other financial policies lose their character as instruments for the fulfilment of innumerable specific targets handed down to enterprises in the form of directives. Instead, the main emphasis is placed on the ability of the Government to adapt its financial and fiscal policies to a much more mobile environment and to intervene quickly and efficiently in sectors where the emergence of imbalances threatens over-all financial equilibrium and jeopardizes the implementation of the general objectives of the plan. Such intervention will consist mainly of the application of various "fiscal and financial instruments", and the use of financial reserves which, according to prevailing views, should be constituted at the central level.

[4] Thus, for instance, the new Polish five-year plan envisages a considerable expansion of the network of savings institutions, especially in the countryside. See *Nowe Drogi*, No. 2, 1967 (Warsaw), pages 33-34.

The creation of strategic financial reserves expressedly designed to ensure a quick elimination of imbalances acquires crucial importance in the new conditions.[5]

The increasing role of profit consideration as the determinant of the activities of enterprises implies a very significant change in the nature of the budgetary revenue from profits. Under the old system, these revenues, called "deductions from profits", represented in fact a direct transfer of the bulk of the enterprise profits to the budget. The amounts of these transfers were stipulated for individual enterprises annually in absolute terms, and were as obligatory as other directive targets assigned to them by their supervisory authorities. The central ministries were responsible for the transfer of these sums to the budget along with the proceeds from turnover tax included in their receipts.

The reduction of the role of directives as the basic means of implementation of plans should, according to widely held views, lead to the replacement of the deductions from profits by a tax imposed on profits at a specified rate. The importance of this change, already introduced in Czechoslovakia, is that the planned revenue from profits ceases to be an obligatory directive fixed in absolute terms and broken down by ministries, and becomes a budgetary estimate comparable to similar estimates in countries under a different economic and social system. It will be remembered that, under the new system, this tax as well as other long-term economic instruments is to be established for the duration of the medium-term plan. As these policies will have to be taken into account in the preparation of annual fiscal budgets, it is clear that these budgets will be less dependent on the objectives of the annual economic plan than was the case in the past. In fact, the formulation of the annual economic plan itself will be to a certain extent influenced by the budgetary estimates which, in the new conditions, are in part determined by the fiscal and financial parameters of the medium-term plan.

If the estimated budgetary revenue proves to be smaller than the financial implications of the preliminary draft of the annual plan, this may lead to the revision of original targets in conformity with financial possibilities. Only in cases where such revision would imperil the achievement of the main objectives of the medium-term plan would additional financial resources be mobilized by the use of supplementary measures, on a temporary basis.

[5] It is generally recognized that these reserves should be much greater than the amounts now allocated for this purpose, which are no more than about one half to one per cent of the budget. Even under the conditions of directive planning, these reserves frequently proved smaller than necessary and, in some cases, were exhausted soon after the beginning of the budgetary year.

FINANCIAL PLANNING AND MEDIUM-TERM PLANS

Notwithstanding the broad similarities between annual and medium-term financial planning, the role and nature of the latter offer certain specific features which are more conveniently discussed separately.

The essential difference between annual and medium-term plans is, as noted previously, that in centrally planned economies only annual plans are fully operational. It is through the annual plans that the targets of the medium-term plans are translated into operational decisions. One of the main functions of the annual financial plans and balances was to provide a basis for issuing financial directives to operating units. In contrast, the financial balances used in medium-term planning were never aimed at the formulation of any operational directives. Their essential function was to disclose the existence of eventual imbalances in the preliminary drafts of the national economic plans and to suggest the necessary corrections before their final approval. The medium-term financial balances are conceived only as "working documents", and are drawn up in a highly aggregated form. They are not generally presented to all interested ministries, and because of their nature as subsidiary documents they are not submitted to the ratification of the state authorities.

Although the aggregate balances include various items of a budgetary nature, their elaboration has never taken the form of a state budget or budgets for the period covered by the medium-term plan. It is true that, in the early period of planning, in some rather isolated cases, the national economic plan did contain certain estimates of budgetary requirements broken down into broad categories of expenditure for the five-year period[6] or for the terminal year of the plan.[7] Even in these cases, however, it was explicitly stated that the actual budget need not conform to the estimates, provided that the economic targets of the plan were met.[8] This attitude towards the role of budgetary estimates in medium-term planning was also reflected in the belief that, in view of the highly conjunctural character of medium-term financial estimates, there was no need to include in the plan any specific "budgetary guidelines" designed to keep the growth of budgetary expenditures and revenue in line with the basic assumptions of the national economic plan. The limitations imposed by such guidelines could hardly be of much use for the medium-term plan, at least in the highly centralized system prevailing in the

[6] See, for example, Eastern Germany, Amt fur Information, *Gesetz über den Fünfjahrplan* (Berlin, 1 November 1951).

[7] This was the case with the second Soviet five-year plan.

[8] For a very explicit formulation of this thesis, see *Finanse,* No. 11, 1959 (Warsaw), page 4.

centrally planned economies prior to the introduction of the recent reforms. In these countries, medium-term economic plans contained aggregate and sectoral targets for output and investment as well as for productivity and wages, which implicitly determined the requirements for, and sources of, savings, the main portion of which was derived from the enterprise sector and transferred to the budget. In these conditions, it was felt that the introduction of specific budgetary guidelines would merely impose additional constraints, without providing policy makers with any more effective means of implementation.

The transition to the new methods of plan implementation will have a considerable impact on the role of financial planning in the context of medium-term economic plans. This role will no longer be largely confined to testing the internal consistency of these economic plans but will become increasingly important for the formulation of medium-term financial policies adapted to the objectives of medium-term plans.

This new function of financial planning in Czechoslovakia has been clearly defined in a statement according to which,

> "the purpose of the financial planning is not so much to fill in the individual positions of the five-year financial plan—which incidentally is not subject to government approval—as to ensure the achievement of the basic proportions and the postulated level of effectiveness and profitability, in conditions of economic equilibrium".[9]

According to the same source,

> "an important role in the new system of management will be played by the so-called economic regulations, by which we understand, *inter alia*, the principles of policy concerning financing, credit, interest rates and turnover taxes, and a particularly important instrument, the principles regulating the transfer of profits or of gross income of enterprises to the budget".[9]

The need to establish such "financial instruments" for the medium-term period follows to a large extent from the fact that in the new conditions it is no longer possible to rely on the rather simplifying assumption of quasi-automatic links between production, productivity and wage targets on the one hand, and the budgetary accumulation of funds for investment and social consumption on the other. Under the new system, such assumptions are losing whatever validity they possessed in the past in so far as the number of plan targets translated into operational directives is being reduced. It will be remembered that the gradual extension of the operating units' freedom of decision relates not only to production but also in varying degree to wages, profits and even, to an increasing extent, prices. Moreover, all the reforms envisage increasing the proportion of profits left at the disposal of enterprises.

It is clear that in these conditions it can no longer be assumed that, for example, the fulfilment of output and productivity targets will lead almost automatically to the accumulation of savings in the amount required to finance the investment programme. The process of decentralization weakens the link which, in the past, could be established directly—at least in the planning stage—between production, savings and investment plans. Furthermore, under the new system, the role of financial and fiscal policies acquires new dimensions in so far as their new function is to replace administrative directives as the principal instruments whereby enterprises may be induced to act in conformity with the main objectives of the development plan. All these changes considerably reinforce the need for broadly formulated medium-term policies in regard to taxes, credits, prices, wages and profits, necessary not only for the attainment of the planned level of savings but also for the implementation of the main objectives of the plan.

The formulation of such policies, on the basis of the analysis of the plan's financial implications and prospective developments in the field of finance, may lead to the conclusion that for political or economic reasons the required changes in taxes, credits and income distribution cannot be achieved. This in turn may lead to the revision of certain targets outlined in the preliminary draft of the medium-term plan.

It is clearly not accidental that increased emphasis on medium-term financial planning has always coincided with proposals for significant changes in prices and wages or with the introduction of measures intended to increase the scope of autonomous decision making by enterprises. Thus, for instance, special attention was devoted to medium-term financial problems in the preparation of the post-war reconstruction plans, generally covering a three-year period, which in some cases laid down in broad outline prices, wages and taxation policies for the whole period.[10] Similar preoccupations again became apparent in the late 1950's when the introduction of certain measures of decentralization raised various problems of financial policy. The first attempt to develop an integrated system of financial policy measures for the duration of a medium-term plan was made in Czechoslovakia in 1958 in connexion with the preparation of the five-year plan.

The purpose of the Czechoslovak experiment was to increase the freedom of decision of enterprises

[9] See *Deutsche Finanzwirtschaft*, No. 15, 1965, page 21.

[10] The need for the formulation of such policies was also made necessary by the existence at that time of a relatively large private sector.

in the field of financial operations. Considerable funds were left at the disposal of enterprises, mainly for investment purposes, and the enterprises were given an assurance that a further rise in their profits would not lead to an increase in the profit tax rates during the period of the medium-term plan. This was achieved by establishing a system of norms fixing the share of the profits left at the disposal of enterprises for the duration of the medium-term plan. Similar norms were established with respect to depreciation funds. Moreover, enterprises were also freed from directives concerning wages, which were replaced by norms relating the growth of wages to that of productivity. For reasons outside the scope of this study, the 1958 experiment was not successful and had to be abandoned.

The recent economic reforms have again brought the problems of medium-term financial planning into sharper focus. This has been reflected in numerous debates and studies concerning the role of medium-term financial planning, and more important, in the formulation in some of the eastern European countries of various financial provisions within the framework of medium-term plans. Thus in Czechoslovakia, where the role of directives in plan implementation was virtually eliminated in 1967, the drawing up of financial plans and balances played an important part in the preparation of the new five-year plan for 1966-1970.

The use of financial balances in the process of preparing the medium-term plans under the new system may be illustrated by the example of Czechoslovakia where the new approaches were used in the elaboration of the plan for 1966-1970. The considerable increase in the role of medium-term financial planning under the new system was first reflected in the preparation of much more detailed financial balances. While, in the past, medium-term plans and balances had been set up chiefly in the form of a highly aggregated "financial balance of the national economy" or of the state sector only, the new system, which involved a considerable degree of financial autonomy of various producing units, required a much more detailed analysis of prospective financial flows. This was needed not only for consistency tests but also, and primarily, for the formulation of medium-term policy parameters, especially in the field of taxation, and for the establishment of rules and regulations governing the use of financial resources of the enterprises.

In view of this, the "model of aggregate financial relations", formulated for 1966-1970 and broken down into annual segments of the five-year plan, contained, in addition to the state budget, credit plan and the financial account of the state enterprises, also more detailed accounts for the co-operative sectors, the non-productive sector, foreign trade and the household sector. The account of the "state economic organizations" was divided into subgroups according to the type of financial rules and regulations to which they were subject.

According to a recent report,[11] the analysis of the prospective financial balances conducted in the process of preparing the 1966-1970 plan has indicated that, for the period taken as a whole, the plan is internally consistent and that the financial resources required for its implementation are balanced by the revenues. But the financial accounts drafted for each year of the five-year plan have indicated considerable potential imbalances for individual years. It has appeared, in fact, that while the financial requirements for investment and social consumption implied in the preliminary draft of the plan were in excess of anticipated revenues during the initial years of the plan, the reverse was true for the last years of the five-year period. This pattern of anticipated changes was largely the effect of a widespread tendency to concentrate investment in the initial years of the plan, notwithstanding the fact that the volume of potential saving is, *ceteris paribus,* much greater at higher levels of income reached in the concluding years of the plans than at the time of their inception. Moreover, the more detailed analysis of these flows has disclosed that the developments implied in the physical and financial aspects of the preliminary draft of the five-year plan will result in a deficit in the state budget and in a considerable accumulation of liquid assets in the hands of the enterprises. The use of these assets for additional spending, over and above the amounts anticipated in the plan, would generate inflationary pressures if their effect were not compensated by a reduction of the budgetary deficit, by the tightening of credit or by an increase in the supply of goods and services over and above the original targets.

The main purpose of this analysis was to provide a background for the formulation of policies for preventing the diversion of real resources from the uses considered to be essential for the fulfilment of the main objectives of the five-year plan. The ensuing recommendations may deal with such problems as medium-term fiscal and credit policies, encouragement of saving, rules and regulations governing the allocation of net proceeds among various enterprise funds, as well as with the need for fuller utilization of existing reserves, for raising output and supplies to the levels required by the anticipated demand.

The considerable increase in the role of medium-term financial planning under the new system was

[11] See *Planované Hospodarstvi* (Prague), No. 10, 1966, pages 1-8.

reflected primarily in the extensive use of financial balances for the formulation of medium-term policies and regulations covering a wide area of financial flows and transactions. As already mentioned, the need to determine these policies for a prolonged period is based on the belief that a certain stability of financial and fiscal parameters is necessary for the efficient operation of the enterprises and other producing units. This does not, of course, preclude the introduction of similar or additional measures and regulations within the context of annual plans. It is, however, increasingly recognized that medium-term plans provide a much more adequate framework for decisions concerning general regulations, as well as for fiscal and financial policies which may be required for the fulfilment of those plans. This new attitude towards medium-term financial planning does not imply, however, the need to formulate binding budgetary guidelines in the form of targets for, or ceilings on, various types of budgetary expenditure and revenues. It is generally believed that the establishment of such restraints would introduce undesirable rigidity into the system and prevent the adaptation of budgetary policies to current requirements. It has been pointed out in this connexion that the absence of any rigid budgetary commitments in the medium-term plans of the centrally planned economies has left the door open for various short-term adjustments that may be called for by the current financial situation. Such adjustments have, in fact, frequently been made in the course of executing the plans and have led to considerable changes in the financial parameters assumed to be realistic at the time of their formulation.

It is generally considered in the centrally planned economies that these views, based on past experience, retain their validity under the new system of planning and management. They have also been supported by the recent experience of Yugoslavia. While the Yugoslav plan for 1961-1965 contained budgetary targets broken down into broad categories of expenditure, no such targets were included in the new five-year plan for 1966-1970. The new federal plan contains only one indication regarding budgetary expenditure: it states that the capital and current expenditure on administration and defence is expected to decline from 6.5 per cent of national income in 1965 to 5.3 per cent in 1970. The plan does, however, contain several decisions regarding fiscal and financial policies believed to be indispensable for the fulfilment of the main objectives of the medium-term plan; these decisions are binding on the Ministry of Finance and the National Bank. Some of the measures are rather general in character. They can be exemplified by the provision prohibiting the financing of deficits in the federal budget and the social security system by borrowing from the National Bank. Other stipulations are much more specific; the most important among them determine the share of budgetary participation in the financing of several projects listed individually in the plan or in its subsidiary documents. The formulation of this type of policy measure, both general and specific, is considered to be more effective as regards plan implementation than attempts to fix rigid targets or ceilings for all budgetary receipts and expenditures for the period covered by the medium-term plan.

Chapter VII

PROBLEMS OF THE PREPARATION AND IMPLEMENTATION OF INVESTMENT PROJECTS

One of the features of investment plan preparation in the centrally planned economies has been that the starting point is the evaluation of the investment required to achieve planned output targets, rather than the elaboration of individual investment projects. Projects are chosen not on the basis of their individual profitability but entirely in acordance with their impact on the achievement of the desired pattern of growth.

"Efficiency criteria" were, of course, extensively used in choosing between alternative projects producing the same type of goods or substitutes for them. The criteria were used to select projects possessing the optimal combination of factors of production under prevailing conditions. It was generally believed, however, that criteria of this kind should not be used in choosing between investment projects in different branches of industry. According to these views, the well-known difference between the marginal net product of an industry and its social net product makes it imperative to disregard the profitability of individual undertakings as a guideline for the sectoral or branch allocation of investment.

There are two important points to be stressed in this connexion. First, according to widespread opinion, the foregoing statement holds chiefly in cases where the purpose of development planning is to bring about profound structural economic changes which cannot be achieved through the free play of market forces. Secondly, in its general form, the statement cannot be applied to projects connected with foreign trade. It will be realized that, in this case, the concept of the planned target—future foreign currency earning or saving—is much broader than in the domestic comparison of projects, because it admits not only the choice between various techniques of production of a given commodity but also a choice between investment in various industries, provided that they are linked with foreign trade.[1] In consequence, efficiency criteria have been utilized in decisions concerning the expansion of domestic production or imports of certain commodities as well as production of other commodities for exports. It should be added, however, that the results of such analyses were not regarded as sufficient for a final decision. Two other considerations came into play at this point, one concerning the foreign demand for exports and the foreign supply of required imports, and the other concerning the advisability of increasing dependence on imports of goods considered strategically important from the economic as well as the military point of view. In any event, decisions influenced by these evaluations were reflected in the production targets which provided the basis for the sectoral allocation of investment.

In the preliminary stages of investment plan preparation, requirements for additional capacity have been evaluated by means of the application of broadly estimated capital-output ratios to production targets. The feasibility of investment programmes has been tested by using balances of the supply of labour, building materials and the machinery and equipment required for the implementation of the plan. Requirements for these goods and services have also been based at this stage on general estimates of broad aggregates rather than on the evaluation of specific projects. The results of these estimates have been further compared with the anticipated domestic supply of the required goods and the possibility of imports, and after a complex process of multiple adjustments of various production and investment targets they have been used for the formulation of an investment programme co-ordinated with the production and supply targets set for the period covered by the plan.

This preparatory work has been mainly carried out by the central planning agency, which provides the executive bodies, such as the industrial and other ministries, with preliminary estimates of the investment funds which may be made available to them. The final decisions are arrived at only after consideration of the suggestions and requests made by the ministries to the central planning agency.[2] This

[1] For a detailed description of these techniques, see *Economic Survey of Europe in 1962: Part 2—Economic Planning in Europe* (United Nations publication, Sales No.: 65.II.E.4).

[2] It will be remembered that the preliminary investment targets or "limits" are transmitted in an increasingly disaggregated form from the higher to the lower executive agencies and operating units. These agencies and units formulate their own counter-proposals, which, after appropriate correction by their supervising authorities and the central planning agency, are used in the formulation of the final investment "limits" for each operating unit.

does not mean, of course, that the participation of ministries and enterprises in the planning process starts only after they have received preliminary indications from the planning agency. In fact, even the preliminary evaluations of investment needs are prepared in close co-operation with the industrial ministries. In view of their responsibility for the development of the industrial branches under their supervision, investment planning for these ministries is not a single act performed at the time of the presentation of the plan but a continuous process conducted by their own planning units, scientific institutions and other organizations.

The investment planning of executive agencies and enterprises is obviously not limited to broad evaluations of their need for investment funds. The largest part of it consists of the preparation of specific projects initiated independently or suggested to them by the planning authorities. At any point in time, the ministries have under consideration a number of projects in various stages of preparation, which can be used for the evaluation of their investment needs and for submitting their proposals to the central planning agency.

Not all projects prepared by the ministries are listed individually in the national plans. The lists include only projects above a certain value, which in view of their importance are defined in some detail as to cost, capacity, location and other characteristics, as well as time schedules for the various stages of their construction. Investment outlays for the remaining projects are indicated in the national plan only in the form of aggregate sums broken down by ministries without reference to individual projects. Approval of these projects and the allocation of funds among them remain within the competence of the individual ministries which submit only a general justification of their financial requests to the central planning agency.

The type of documentation required for the inclusion of projects in national or ministerial medium-term plans is very different from that needed for annual plans. Since at the time when the medium-term plan is prepared, the basic question is whether the project is justified from the point of view of the plan's general objectives, the documents used for this purpose are much more general in character than those required for operational decisions. In consequence, at this stage, documentation for a project must include a justification of the need for the project in the development of a given branch in accordance with the plan, a description of the technical processes to be used and the technical equipment required, the composition of the completed project's output, its feasibility, import requirements, links with interrelated projects, and time schedules for its construction and, of course, its estimated cost.[3]

In practice, however, projects included in the medium-term plan vary considerably with respect to the degree of preparation reached at the time of their presentation to the central planning agency. The experience of the centrally planned economies indicates that it is hardly possible, at this stage of the planning process, to have a fully elaborated set of projects corresponding to the total investment planned for the medium-term period. In consequence, the main effort has been concentrated on the preparation of major projects and on projects scheduled to begin during the initial years of the medium-term plan. The remaining projects were to be elaborated further in the course of the plan's implementation. The planning authorities of the centrally planned economies have of course been aware of the fact that important modifications in the original projects might adversely affect the balance between supply and demand for investment goods and services as well as other economic relationships outlined in the plan. This has been accepted, however, as an unavoidable risk worth taking in view of other considerations which will be indicated later. In consequence, a significant proportion of projects have been incorporated in the medium-term plan without completely adequate documentation.

Projects included in the annual plans have to be presented in a much more advanced stage of preparation than is required for the medium-term plans. This is due to the fact that in this case the problem is no longer one of deciding whether the project is justified but whether its preparation has reached the operational stage. At this point, investors, whether associations of enterprises or individual enterprises, are required to have ready complete blueprints, technical details regarding construction work, a list of the machinery and equipment required for the project, and a precise evaluation of the cost of every stage of its implementation. The most important other requirement is the investor's obligation to demonstrate that the delivery of goods and services needed for the construction of the project has been ensured by agreements concluded with building enterprises and suppliers of machinery and equipment.[4] As a rule, this documentation is presented to the ministries responsible for individual sectors or industrial branches, which then submit their requests to the central planning agency.

[3] It also includes comparisons of the costs, technological processes, equipment, and over-all efficiency of the project with those of similar undertakings within the country and abroad.

[4] For a large proportion of goods and services, such contracts can be signed only with enterprises expressly designated by the agencies responsible for the allocation of supply.

The experience of the centrally planned economies shows, however, that as in the case of the medium-term plan the conditions governing the inclusion of projects in annual plans could not be fully respected. Although considerable efforts were made to induce investors to submit fully documented requests, a large proportion of projects were in fact included in the annual plans without these requirements being met. This practice, deplorable as it may appear, was largely explained by the reluctance of ministries and planning agencies to exclude from the annual plan projects of vital importance to the fulfilment of the medium-term plan, on the grounds that they were not fully prepared. It is not, indeed, always possible to say whether the loss to the economy caused by postponing the construction of various projects is not much greater than the additional cost incurred by starting construction before fully elaborated documentation is available. This consideration is particularly important in the case of interrelated projects, because of the risk of a chain reaction affecting a large area of productive activity in various sectors of the economy.

This is not to say, of course, that this state of affairs is regarded as tolerable. It means only that the problem cannot be solved simply by automatically excluding all inadequately prepared projects, irrespective of their importance to economic growth. A more selective approach would take into account, on the one hand, the impact of exclusion on the implementation of the medium-term plan, and on the other the possibility of initiating the first stages of construction of a given project on the basis of available documentation, to be completed later.

It is, however, stressed that a real solution to these problems should be sought in the creation of conditions which will induce investors, as well as design and construction enterprises, to concentrate their efforts on improving the preparation and implementation of investment projects. It is generally agreed that in the past such inducements were virtually non-existent and that this fact was largely responsible for the shortcomings observed in this field.

The main shortcomings in this area of economic activity were in many ways similar to those encountered in other countries regardless of their economic and social system. Apart from the delays in the preparation of projects, the actual cost was often much higher than estimated, the construction period was much longer, the type of equipment indicated in the original designs was changed in the process of implementation, and the goods and services needed by the projects were not delivered on time or in the volume and quality required. Some of these shortcomings can be illustrated by the following examples. According to a survey carried out by the Central Statistical Administration of the USSR, the actual construction period of 147 projects covered by the investigation was one fifth to twice as long again as planned. Not one of these projects was completed within the period corresponding to the "normative" time-schedules used in preparing the plans.[5] In Hungary, of 617 major projects built during the second five-year plan, 34 per cent were completed according to the planned time-schedules; 25 per cent were completed and put into operation with a delay of two to five years. Quantifiable losses due to these delays were equivalent to about 10 per cent of total investment during 1961-1965.[6]

Differences between the estimated and actual cost of investment projects were quite large in all the centrally planned economies. In the Soviet Union, a survey of 475 major projects by the State Committee for Construction disclosed that the actual cost of these projects exceeded by 25 per cent the cost estimates approved by the relevant agencies at the time of their inclusion in the plan.[5] A similar survey conducted in Hungary showed that the cost of more than one half of the projects completed in 1963 was considerably higher than planned.[7]

Some indication of the factors responsible for cost increases over and above the original estimates is provided by the following evaluation of their relative contribution to increases in costs on 600 construction sites in the Russian Soviet Federal Socialist Republic in 1966. According to these estimates, 38 per cent of the increment in total cost was due to miscalculations by construction and design enterprises; increases in the cost of equipment and in current unit costs and overhead were responsible for 13 per cent of the increment in total expenditure; 11 per cent of the increment was caused by a change-over to more expensive forms of construction and materials, and 25 per cent of the increment was accounted for by changes in the originally approved blueprints and designs.[8]

In interpreting these data, it should be remembered that they do not cover all the projects under construction, large numbers of which were executed efficiently. Furthermore, the lack of comparable data makes it difficult to ascertain whether the magnitude of the problems encountered in project construction in the centrally planned economies is different from that encountered in other parts of the world.

The preceding account shows that the efficiency of investment activities in the centrally planned economies suffered from both the inadequate preparation of investment projects at the time of their

[5] *Voprosy Ekonomiki,* No. 7, 1965 (Moscow).
[6] *Népszabadság* (Budapest), 15 January 1967.
[7] *Pénzügy Szemle,* No. 8-9, 1965 (Budapest).
[8] See V. O. Cherniavsky, *Ekonomika Proektirovania i Stroitelstva v Novykh Usloviakh* (Moscow, 1966).

approval and shortcomings in their implementation. While the reasons for these difficulties were analysed in these countries long before the introduction of the present reforms, and certain remedies were suggested and introduced, all of them have been subject to much closer scrutiny in connexion with the new reforms.

In the following paragraphs, an attempt is made to present the views that have been expressed in recent debates on the causes of these difficulties and on the remedies suggested or applied in recent years.

According to these views, the root of the problem lies in the system of management which prevailed in these countries prior to the recent reforms. Under that system, decision making in regard to most investment projects, the allocation of materials, equipment and labour, and the choice of design and construction organizations, was concentrated in the hands of the central authorities. Inasmuch as most investment funds were made available to investors[9] in the form of free budgetary grants, there was little inducement to save on investment outlays and to improve the utilization of existing capacity. In these conditions, investors tended to maximize their investments, irrespective of their actual needs. Moreover, in order to "get a foothold" in the investment plan, the investing units frequently understated the cost of projects submitted for approval. This was done in the not unjustified hope that the supervising authorities would be reluctant to abandon the project after its initiation because of the resulting waste of the funds already invested. It is quite obvious that these practices were made possible by the lack of financial responsibility of the investing units.

The tendency to underevalution of cost was also reflected in understatement of the physical amounts of materials, equipment and labour required for project construction. In consequence, the cumulative effect of such underevaluations was an important factor undermining the reliability of the balances between the supply and demand for investment goods and services. These practices were, apart from the overstrained investment plan, an important factor accounting for almost continuous excess of actual demand over supply in the field of investment activities.

Another cause of these imbalances was directly related to the techniques used in the preparation of investment projects. The cost estimates and the requirements for materials, equipment and labour indicated in the project documentation were as a rule calculated on the basis of information concerning the performance of similar projects built with the use of highly advanced techniques within the country and abroad. The aim of these methods was to bring about, by administrative measures, improvements in the quality and efficiency of projects at the preparatory stage. Unfortunately, the standards and norms used for the preparation of projects were frequently far removed from the actual conditions[10] and their utilization gave rise to requirements which could hardly be met by the operating units. This was true also with respect to cost estimates based on price-lists and catalogues, which were frequently out of line with the actual current cost of goods and services.

The general conclusion which arose out of the analysis of the difficulties encountered in the investment field was that they were the result, on the one hand, of overstrained investment plans, and on the other of defective methods of preparing and implementing investment projects. Many of these shortcomings were, it is believed, largely the effect of over-centralization and lack of incentives to greater efficiency.

Within this broad area of agreement, however, there are significant differences in the emphasis placed on each of these factors. According to some views, the main cause of the difficulties was the excessive volume of investment, due not so much to deficiencies in the preparation of investment projects as to political decisions by the central Government. Many defects in the work of design and construction enterprises were the direct result of excessive demands imposed upon them by the investment programme. Thus, for example, the dispersion of the activities of construction enterprises over an excessive number of projects had resulted in work interruptions caused by shortages of labour, materials and equipment, and consequently in considerable delays and increases in cost. According to these views, a less ambitious investment plan would in itself be sufficient to improve the situation. The ensuing reduction or elimination of relative shortages of investment goods and services would have an immediate effect on the activities of the enterprises responsible for preparing and implementing investment projects.

However, according to prevailing opinion, a more realistic formulation of aggregate investment plans would not be sufficient to solve the problems discussed above. Moreover, it has been stressed that there can

[9] In the centrally planned economies, investors in the sense used in this chapter are state enterprises already in existence or, if the project is to be built for a newly created enterprise, the association to which the new enterprise will be subordinate or a specially formed unit representing a nucleus of the managing body which will take over the enterprise after its completion. In the non-productive sectors, government agencies act as investors in the areas under their jurisdiction.

[10] Such as organization and technique of construction work, productivity of labour, conditions of supply of building materials and equipment.

hardly be any significant improvement in the investment policy of the central authorities without far-reaching decentralization, which would involve greater freedom of decision for all the participants in the process of the preparation and implementation of investment projects and a considerable increase in the role played in these decisions by profit considerations.

The need for improvement in the field of preparing and implementing investment projects was recognized in all the centrally planned economies long before the initiation of the present reforms. However, the remedies suggested or introduced at that time in most of these countries concentrated on the elimination of certain specific shortcomings and had a relatively limited effect on the broader issues indicated above. Thus, for instance, in several of the centrally planned economies, particularly the Soviet Union, it was suggested that the "normative" indicators used in the preparation of projects should be improved by the introduction of corrective coefficients derived from discrepancies between the planning "norms" and actual relationships between various factors observed in the past. While the need for such improvements was generally recognized, the new approach has seldom been applied in practice.

Several improvements were also suggested in the system of rewards and bonuses for enterprises participating in the preparation and implementation of projects. Thus, for instance, a special bonus paid to designing agencies for innovations reducing the total cost of new projects proved to have a detrimental effect on the work. In order to increase their rewards, the agencies tended frequently to achieve cost reduction at the expense of the quality of the construction and equipment designed for the new project. Because of this, it was suggested that this type of bonus should be discontinued.

The methods employed to secure the implementation of plans by building enterprises and the system of payment for their work were also strongly criticized. The system of valuation of various types or stages of construction carried out by building enterprises that was used for measuring the degree of plan fulfilment and for payments to the building enterprises was not commensurate with the work actually done. Consequently, the construction enterprises tended to concentrate on building those parts of a given project which were for them most advantageous, regardless of the required sequence and the time-schedules established for the various operations. Since at more advanced stages of construction the same "volume of work" required more time and labour, building enterprises were inclined to neglect the completion of projects under construction in favour of beginning new ones. Among various proposals for eliminating these defects, which were one of the causes of the exceedingly high volume of unfinished construction in the centrally planned economies, the most significant was a recent suggestion that was already in line with the new economic reforms. Under this proposal, building enterprises would not be paid for their work until the project or its main components was completed. In the meantime, their current expenses would be financed by interest-bearing loans. These measures, already partly introduced, will, it is believed, eliminate the defects of the old system and induce the construction enterprises to reduce considerably the time actually spent on the completion of investment projects.

Several measures along these lines, already taken by most of the eastern European countries, tend to increase the financial responsibility of state enterprises and by this means to improve the preparation and implementation of investment projects. One of these measures is the tax on fixed assets which is used to induce enterprises to improve the utilization of existing capacity and thus to save on new investment projects. Another much more important measure, although not yet fully in effect, is the replacement of budgetary investment grants by interest-bearing loans. Obviously the full impact of these measures on the preparation and implementation of investment projects can only be realized within the context of the much broader reforms. The purpose and content of these reforms were reviewed in the preceding sections of this chapter, and in the present context only a few additional points, concerning investment projects, need to be made. As already mentioned, in most centrally planned economies, with the notable exception of Czechoslovakia, the sectoral allocation of investment will continue to be determined by the national plan. Decisions concerning individual investment projects, however, will increasingly be left to the investors, who will bear full financial responsibility for their decisions. Under the new system of planning and management, when it is fully developed, the investor will have an opportunity to make a free choice among design and building organizations. The gradual elimination of the central allocation of the supply of investment goods will enable the investor to enter into freely concluded agreements with other enterprises concerning the delivery of machinery and equipment for new projects.

It is generally believed that these institutional changes, together with improved adaptation of investment plans to the supply of investment goods and services, will eliminate most of the present shortcomings in the field of the preparation and implementation of investment projects.

SUMMARY

Though the methods of planning and of plan implementation adopted in the centrally planned economies were closely related to political and social conditions prevailing in those countries, some aspects have relevance to the problems of planning in countries with different economic and social systems. Until recently, hardly any transfer of experience was possible in plan implementation, since in the centrally planned economies this was largely achieved through administrative order. The changes in methods of plan implementation currently taking place in the centrally planned economies, involving as they do increasing reliance on market forces and genral economic incentives, are tending, however, to enlarge the area of common interest amongst countries despite differences in their economic and social systems.

Despite the important changes in methods of planning and policies of implementation in the centrally planned economies, certain common features have permeated government attitudes to planning at all stages of their development. The most significant among them is the belief that the introduction of development planning implies recognition of the fact that the spontaneous operation of market forces is not capable of bringing about the desired acceleration of economic growth and achieving the necessary structural changes. In consequence, in the initial stages of industrialization in particular, vigorous government intervention is necessary. This intervention should not be limited to sectors directly subordinated to the central authorities but should directly or indirectly influence all sectors of the economy. Moreover, since it is believed that the required structural changes cannot be brought about by the free play of market forces, it is maintained that government policy cannot be effective if it is limited to global measures in circumstances in which changes in the structure of the economy are of paramount importance. In consequence, Governments are bound to have recourse to selective policies involving preferential treatment of certain sectors or industries, which, depending on circumstances, might take the form of direct controls or of incentive and disincentive measures applied in a differentiated form to various industries. Since the main function of national planning is to integrate development policies into a coherent system, the scope of the plan should be as broad as the area of government intervention.

In view of this attitude towards development plans as programmes of action, the formulation of all-embracing plans, without regard to the ability or will to implement them, has always been considered as a pointless and misleading exercise. However, the lack of immediately accessible means of implementing comprehensive plans has not been regarded as sufficient reason to accept more narrowly based plans permanently. Instead, efforts have been directed towards attaining the conditions necessary for the implementation of policies covering all sectors of the economy. The precedence of action characteristic for this attitude towards planning has also been reflected in the conviction that the application of a vigorous development policy need not be postponed until adequate data are available for drawing up all-embracing and fully elaborated plans.

According to prevailing views, the contents of the plans and the methods of their implementation should vary according to the main strategic objectives of development policies at various levels of industrialization. Thus the need for far-reaching structural changes at lower levels of development requires more stringent government controls and regulations than may be necessary at higher levels of industrialization. It was the attainment of a higher level of industrialization and the need to adjust the methods of planning and implementation to the new conditions that were the main arguments in favour of the present economic reforms. These reforms consist in a gradual reduction of the use of administrative directives as the main tool of plan implementation. Instead, the Governments will tend increasingly to induce enterprises to act in conformity with the general objectives of the plan by means of fiscal, financial and price policies, whose purpose is to create conditions for bringing the interests of individual enterprises into conformity with the social goals reflected in the plan.

The reduction of the number of directives given to enterprises, and in some cases their virtual elimination, increases considerably the role of profitability of individual enterprises as the determinant of their activities. In earlier periods of development of the centrally planned economies, the profitability of individual enterprises was largely disregarded and the role of market forces was considerably suppressed, on the grounds that the desired structural changes were, in prevailing conditions, contrary to the natural tendencies of the market mechanism. It is now believed that while the directive methods have yielded considerable results, they have been losing

their usefulness and becoming increasingly harmful to further growth as the centrally planned economies have been reaching higher levels of industrialization. This is mainly due to the fact that the gradual exhaustion of the unused material and human resources has led inevitably to a shift of emphasis from "extensive" to "intensive" patterns of growth, relying upon increases in the over-all efficiency of economic activities. It is generally believed that in the new conditions this can be more effectively achieved by stimulating the initiative of the enterprises through a reduction in scope of direct controls and placing greater reliance on the market mechanism.

The enlargement of the role of the market mechanism is not tantamount to the downgrading of the role of central planning and government intervention in economic processes. It does, however, involve significant changes in the content of the national plans and most of all in the methods of implementation. At the present stage, considerable differences exist among the countries with respect to the relative roles of direct and indirect means of plan implementation. Among the many reasons for these differences, one that is frequently mentioned is the importance attached to achieving further fundamental changes in the structure of the economy. Thus, for example, the most radical reforms have been introduced in Czechoslovakia where, according to widely held views, the major need is to secure improved adaptation of production to current demand and higher efficiency of producing units rather than to bring about further fundamental structural changes. In that country, the national plan contains targets for broad aggregates such as national income, accumulation and consumption, which are considered as the basic commitments of the central authorities to which all policy measures should be subordinated. In addition, the plan also contains more specific targets, the implementation of which is considered not as a goal in itself but as a means of achieving the main objectives of the medium-term plan. Most of these targets are defined as "orientation" targets and are not translated into directives for ministries or enterprises. Their main function is to provide information concerning the pattern of changes most desirable for the achievement of the major objectives of the plan. However, if the deviations from the orientation targets risk endangering the general objectives of the plan, recourse is to be had to the use of directives, but only as a last resort after efforts to secure the necessary corrections by the use of various economic instruments have failed. Two types of these instruments are envisaged. The "long-term economic instruments" consist of a system of levies designed to influence investment and wage payment of the enterprises over the medium-term period; as a rule, these are to be applied uniformly to all sectors and branches. The "operational measures" relate to price and wage policies, credit and interest rates, subsidies and additional tax measures and to rules and regulations dealing with the allocations of net revenue of enterprises to various enterprise funds. In contrast to the long-term economic instruments, the operational measures need not be fixed for the duration of the medium-term plan and need not be applied uniformly to all industries or commodities.

A similar system of comprehensive central planning allowing for broad autonomy of enterprises, whose activities are to be guided largely by fiscal, financial and credit policies, will be introduced in Hungary in 1968. In other countries, the number of detailed directives has been substantially reduced but the enterprises are still subject to directives regarding investment, volume and composition of output (expressed in terms of sales), the wage bill and profits. In all cases, however, the role of profitability and of market relations is being increased and, notwithstanding the differences in timing of the reforms and the degree of decentralization already achieved, most of the eastern European countries are moving towards the elimination of directives as the main instrument of plan implementation. It is generally believed that at the present stage of development, the indirect means of influencing the activity of the enterprises may be more effective than plan implementation through administrative directives, provided that these means are sufficiently differentiated to meet the priority rating of various sectors or industries stipulated in the plan.

The transition to the new methods of planning and plan implementation may increase the importance of the inclusion in the plans of clearly defined implementation measures and policies. When all economic activity of enterprises was subject to directives, other implementation policies played a subordinate role. In the new conditions, however, the formulation of price, credit, fiscal and financial policies as well as of rules and regulations governing the activities of enterprises is considered as necessary to enable these units to prepare their own programmes of action on the basis of relatively stable policy parameters.

In all the centrally planned economies, medium-term plans are broken down into annual segments which serve as a basis for the preparation of operational annual plans. In view of their operational character, the annual plans are as a rule more detailed than medium-term plans. In order to ensure that they are operationally valid, much greater participation by the producing units is required in their preparation. Consequently, communication between the higher and the lower echelons, from central planning agencies and industrial ministries all the way down to individual enterprises, is even more important in the preparation of annual plans than in the case of medium-term plans.

The preparation of annual plans is closely associated with the drawing up of financial plans and balances, including the state budget, the main function of which is to serve the implementation of the annual segment of the development plan.

The annual financial plans used in the centrally planned economies consist generally of the following accounts: the state budget, the financial plan of state enterprises, a credit plan, a cash plan and the balance of money incomes and outlays of the population. As a group they reflect the planned financial relations between the budget, state enterprises, other productive sectors, financial institutions and households, and are integrated into a single consolidated "aggregate financial plan of the economy". The purpose of this system of plans and balances, not all of which are equally binding, is to achieve a close co-ordination between the production and other plans and their financial implications. These financial plans and balances were in some countries and at certain periods prepared by the central planning agency or by the ministry of finance, and some of them, such as credit and cash plans, by the central bank. The final co-ordination of all these plans and balances and their integration into the aggregate financial balance of the national economy are carried out by the central planning agency in co-operation with the ministry of finance. It is generally agreed that the pattern of the division of responsibility among various agencies is not of primary importance as long as all agencies co-operate closely with each other. While the budget as well as other financial plans is largely subordinated to the national economic plan, it is not merely a passive reflection of the latter. Even in earlier periods of highly centralized systems of planning, the formulation of financial programmes and of the targets of the plan was conceived of as a two-way process which might lead either to the adaptation of the financial balances to the national economic plan or to readjustment of the economic targets initially included in the plan.

Under the new system emerging from the economic reforms, the role of financial planning will be considerably increased. The greater autonomy of the enterprises, the substantial increase in the share of profits left at their disposal and the fact that their activities are to be largely influenced by fiscal and financial measures rather than by administrative means all combine to give financial planning a new dimension. Although the state budget as well as other financial plans and balances will continue to serve the implementation of the annual economic plans, the establishment of medium-term fiscal and financial policies will make the annual fiscal budgets less dependent on the objectives of the annual plan than in the past. In consequence, the formulation of the annual economic plan itself will be influenced to a certain extent by the budgetary estimates which, in the new conditions, are determined in part by the fiscal and financial parameters of the medium-term plan.

While the annual financial plans and balances served as the basis for issuing financial directives to operating units, the essential function of such balances used in medium-term planning was to disclose the existence of eventual imbalances in the preliminary drafts of the national economic plans and to suggest the necessary corrections before their final approval. Under the new system, the role of medium-term financial planning will no longer be confined to testing the internal consistency of the economic plans but will become increasingly important for the formulation of medium-term financial policies adapted to the objectives of medium-term plans. The purpose of these policy measures and regulations, which cover a wide area of financial flows, is to prevent the diversion of real resources from uses considered to be essential for the fulfilment of the main objectives of the plan. The need to formulate them for the medium-term period is based on the belief that a certain stability of financial and fiscal parameters is necessary for the efficient operation of enterprises and other producing units. This does not of course preclude the introduction of similar or additional measures and regulations within the context of annual plans. This attitude towards medium-term financial planning does not imply, however, the need to formulate binding budgetary targets for or ceilings on various types of budgetary expenditure and revenue. It is generally believed that the establishment of such restraints would introduce undesirable rigidity into the system and prevent the adaptation of budgetary measures to current requirements.

The increased role to be played by profitability considerations in influencing the activity of enterprises is expected to eliminate a large part of the shortcomings experienced by the centrally planned economies in the preparation and implementation of investment projects. The starting point of the preparation of the investment plan has been, and in most countries will remain, the evaluation of investment required to achieve the planned output targets. Projects are chosen not on the basis of their individual profitability but in accordance with their impact on the achievement of the desired pattern of growth. "Efficiency criteria" have been used mainly for deciding between alternative projects producing identical or substitutable goods. The main exceptions have been investments linked with foreign trade, where efficiency criteria have also been used in deciding between projects producing goods for export or goods for import substitution.

More recently it has been stressed that the need to disregard the profitability of individual undertakings as a guideline for sectoral or branch allocation exists mainly in cases where the purpose of development planning is to bring about profound structural changes which cannot be achieved through the free play of market forces. At higher levels of industrialization, however, the sectoral allocation of investment may be increasingly guided by profitability criteria.

In the preliminary stages of investment plan preparation, requirements for additional capacity have been evaluated through application of broadly estimated capital-output ratios, and the feasibility of investment programmes has been tested by using balances of labour, building materials and machinery and equipment. This work has been carried out by the central planning agencies in co-operation with industrial ministries which in turn have been working out their programmes in co-operation with enterprises under their supervision.

At the level of ministries and that of lower operating units, a large part of investment planning takes the form of preparation of individual projects. Only certain of these projects are individually listed in the national plans while others are indicated only in the form of aggregated sums broken down by ministries. The inclusion of specific projects in the plans is subordinated in principle to the presentation of certain documentation setting forth the required information concerning the projects. In practice, a substantial proportion of projects has been included in the medium-term as well as the annual plan, in spite of an inadequate preparation of such documentation. Although the acceptance of inadequately prepared projects and the need for their modification in the process of implementation have entailed considerable losses and have upset the planned balances of supply and demand for investment goods and services, this practice was largely explained by the reluctance to exclude from the plan projects of vital importance to the fulfilment of the medium-term plan, even if they were not fully prepared. It is not, indeed, always possible to determine whether the potential loss to the economy from postponing the construction of a project may not be greater than the additional cost incurred by starting construction before fully elaborated documentation is available. This consideration is particularly important in the case of interrelated projects because of the risk of a chain reaction, affecting a large area of productive activities in various sectors.

The main shortcomings in the field of project preparation and implementation were, apart from delays in the preparation of projects, costs higher than anticipated, construction periods longer than estimated, changes in the design of equipment and difficulties in the supply of goods and services required for the projects. Various measures suggested or introduced to eliminate these shortcomings have had only a limited effect. According to views expressed in recent debates, the difficulties encountered in the field of preparation and implementation of investment projects cannot be solved by partial measures. The main prerequisite for improvement in this field is the further development of institutional changes initiated by the recent reforms. While in most countries, with the notable exception of Czechoslovakia, the branch allocation of investment will continue to be determined by the national plan, decisions concerning individual investment projects will increasingly be left to individual enterprises, which will bear full financial responsibility for their decisions.

The gradual elimination of the central allocation of investment goods and services, together with the establishment of a more adequate pricing system, is expected to create conditions which will enable the investing units to base their decisions on a more realistic evaluation of feasibilities of specific investment projects.

It is generally maintained that these and other institutional changes, together with the improved adaptation of investment plans to the supply of investment goods and services, will eliminate most of the past shortcomings in the preparation and implementation of investment projects.

HOW TO OBTAIN UNITED NATIONS PUBLICATIONS

United Nations publications may be obtained from bookstores and distributors throughout the world. Consult your bookstore or write to: United Nations, Sales Section, New York or Geneva.

COMMENT SE PROCURER LES PUBLICATIONS DES NATIONS UNIES

Les publications des Nations Unies sont en vente dans les librairies et les agences dépositaires du monde entier. Informez-vous auprès de votre librairie ou adressez-vous à: Nations Unies, Section des ventes, New York ou Genève.

COMO CONSEGUIR PUBLICACIONES DE LAS NACIONES UNIDAS

Las publicaciones de las Naciones Unidas están en venta en librerías y casas distribuidoras en todas partes del mundo. Consulte a su librero o diríjase a: Naciones Unidas, Sección de Ventas, Nueva York o Ginebra.

Printed in U.S.A.
17166—August 1967—2,600

United Nations publication
E/4363/Rev.1
ST/ECA/99