Economic Development, Planning, and International Cooperation

THREE LECTURES

by

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Lecture I

PATTERNS OF ECONOMIC DEVELOPMENT

Economic development is increasingly becoming the central theme of economic thought. In the period which started with the end of World War II, the problem of economic development increasingly occupies the center of economic thought. Before that time economic development played a minor role in the thought of economic theorists, particularly among economists of the leading capitalist countries. Their thought at that time was chiefly concerned with problems of economic equilibrium. This was so because development was considered in these countries as something which is taken for granted and which comes about spontaneously, and therefore need not be given special attention.

In more recent times, however, two events occurred which had the effect of making economists conscious of questions of development. One was the development of the socialist countries which started with the Russian Revolution after World War I, the emergence of a number of socialist economies in Eastern Europe, and finally the embarkment of the largest nation in the world, China, on a road of socialist development. These were, in any case most of them, countries which were formerly to a lesser or greater degree underdeveloped, and which after the social revolutions had taken place began to develop in a very rapid way. The most important of them, the Soviet Union, became in a brief period of forty years the second industrial power in the world. This was one factor which drew the attention of economists throughout the world to problems of development.

The other factor was the national revolutionary movements in the countries which formerly were colonial, semicolonial, or in some other form dependent on the leading capitalist powers. The national revolutions, which in a number of countries were victorious, led to the establishment of new independent states or to the emancipation of existing dependent states from foreign political and economic domination. These countries considered economic development and progress to be their chief problem. The international importance of the national revolutions became so great that the whole problem of underdeveloped countries, of their economic progress, became a major, I may say *the* major, international problem. Thus again attention of economists was drawn to problems of economic development. We may say that today economic science is becoming increasingly, so to speak, development-conscious; the theme of development becomes the central theme of economic thought.

As a result of these historical events which I have outlined, we can discern three historic patterns of economic development. One is the capitalist pattern which was followed by the countries of Western Europe and the U.S. The second is the socialist pattern which was started in the Soviet Union, then extended to a number of countries in Eastern and Central Europe, then to China and some other Asian countries. The third is what I shall call the national revolutionary pattern which is establishing itself in countries which emancipate themselves from colonial or semicolonial dependence. In today's lecture, I intend to give a brief comparative analysis of these three patterns of economic development. Before going into that, however, I have to state what is the central issue of economic development.

The essential feature which appears in all these three patterns and distinguishes a developing economy from one which is more or less stagnant in traditional ways of life—

the essential factor of economic development, or in other words, its essential mechanism—is the increase in productivity of labor. This is achieved in three ways. One is the accumulation of part of the product of the economy for purposes of productive investment, the second is technical progress, and the third is the improvement of organization of economic activities. All these three ways of increasing the productivity of human labor are strictly related one to another, appear in every developing economy, and are common to all patterns of economic development. The most important of the three is undoubtedly productive investment.

In the older economies which were stagnant through centuries, or even longer, there existed various obstacles that hampered economic development. These obstacles consisted essentially in the following: the resources available for productive investment were very small. This was so for two reasons. With a low productivity of labor the surplus of produce over what is needed to maintain the labor power of the community was very small. This economic surplus, as I shall call it, was small, but in addition a substantial part, in most cases even the major part of it, was used for non-productive purposes. This non-productive use of the economic surplus was due to the system of social relations, either feudal or in many countries even pre-feudal, as for instance, in some countries of Africa. Under these conditions the amount of economic surplus available for productive investment was very small and this was responsible for the stagnant character of these economies. In addition, the patterns of economic activity were determined by tradition. An economic mentality existed which was not conducive to innovation, to improvement in the technology of production. This further contributed to the stagnant character of the societies in question.

In all the patterns of economic development mentioned, development starts with overcoming these obstacles. This implies overcoming the feudal or pre-feudal system of social relations and the mental traditionalism attached to it. This is necessary in order to be able to utilize a major part of the economic surplus for purposes of productive investment. The removal of feudal or pre-feudal social relations always marks the beginning of economic development; it is common to all the patterns of economic development mentioned above. The difference between the three patterns consists in the way in which these traditional obstacles are overcome and broken down, as well as in the way in which part of the economic surplus is mobilized to serve for productive investment. It is here that the difference in the three patterns emerges.

The oldest of these patterns is the capitalist pattern. Before World War I, it was considered to be the only possible pattern, and one which is universal. It was thought that any country which wanted to enter the road of economic development must repeat this pattern. Such was the unanimous opinion of the leading economists in the old capitalist countries. But even economists who were critical of the capitalist system, and who held socialist views, shared the same opinion. The founders of modern scientific socialism, Marx and Engels, believed that all countries would have to pass through a stage of capitalist development, which is a pre-condition to the development of a socialist society.

What was the essential feature of the capitalist pattern of economic development? The essential feature was capital accumulation and productive investment by the urban middle class. In Western Europe, in the towns, a middle class —the bourgeoisie—developed, which accumulated a certain amount of wealth. Unlike the feudal classes it did not use its wealth for conspicuous consumption but turned it into productive investment. That was the beginning of capitalist development.

Where did the resources for such investment come from? They came from different sources: in the first place from profits accumulated by the merchants who were the first capitalists. These profits were used for industrial investment which soon brought further profits. This again provided a source for new investment. Thus profits from trade and production, partly also from financial operations of the middle class, became the basis of the investment which led to capitalist development. But these were not the only sources. In addition, there were others: one, and a very important one in the emergence of capitalist development, was the exploitation of colonies. Such exploitation frequently took the form of direct plunder, to mention only the great plunder of India. Other forms of exploitation were through trade monopolies. At a later stage capital investment in colonial or semi-colonial countries provided an important source of capital accumulation and productive investment in the countries of Western Europe. It contributed very much to accelerating their economic development. Another source was the ruin of small craftsmen and peasants, whose property was taken over by capitalists and turned into capital.

Finally, a certain amount of capital accumulation was either carried out or facilitated by the state. It should not be forgotten that particularly in the earlier stages of capitalist development, the state played a rather important part, either directly investing in fields such as railroads, public utilities, and sometimes even in industrial and commercial enterprises, or subsidizing private enterprises. Particularly in the construction of what is called the infrastructure or the social overheads of productive activity, the state used to be very active as an investor or in subsidizing private investments. Thus public investment played an important part in the capitalist pattern of development.

Such was the way in which the countries of Western Europe and later the United States of America started upon the capitalist road of economic development. Later, with capitalist enterprise in industry, commerce, and finance already established, the profits derived from these enterprises provided the source of further capital accumulation and self-sustained economic growth.

This process of capitalist development was unequal in various countries. International capital investment came into play as a factor accelerating the development of the less developed countries. In the less developed countries, the rate of profit was higher than in the more developed ones. This provided an incentive for capital movements out of the countries with a greater abundance of capital resources to those where capital resources were relatively scarce. This helped to speed up the development of the less developed countries.

Such was briefly the capitalist pattern of development which, prior to World War I, appeared to economists—and as I said, to economists of all shades of opinion—as a kind of universal law of economic development, a way which all countries must traverse. But we know from historic experience that other patterns of economic development have emerged in the socialist countries and, more recently, in countries which I classified as countries undergoing national revolutions.

We may ask what happened, what made the capitalist way of development impracticable in solving the problems of underdeveloped countries and made these countries embark upon other roads of economic development? The answer is that a new factor entered into the picture. This factor is the development of monopoly capitalism and imperialism. Monopoly capitalism and imperialism made it impossible for the underdeveloped countries to follow the traditional pattern of capitalist development. This is so for a number of reasons. The most important is this: with the development of large capitalist monopolies in the leading capitalist countries, the capitalists of those countries lost interest in developmental investment in the less developed countries because such investment threatened their established monopolistic positions. Consequently, investment in underdeveloped countries of capital from the highly developed countries acquired a specific character. It went chiefly into the exploitation of natural resources to be utilized as raw materials by the industries of the developed countries; and into developing food production in the underdeveloped countries to feed the population of the developed capitalist countries. It also went into developing the economic infrastructure such as transportation, ports, and other facilities needed to maintain economic relations with the underdeveloped countries.

In consequence, the economies of the underdeveloped countries became one-sided, raw material and food exporting economies. The profits which were made by foreign capital in these countries were used not for reinvestment in these countries but were exported back to the countries where the capital came from. Or if used for investment in the underdeveloped countries, they were used for investment in production of raw material, of food, and for construction of an infrastructure. They were not used for industrial investment on any major scale, which, as we know from experience, is the real dynamic factor of modern economic development. This is the essential reason why the underdeveloped countries were not capable of following the classical capitalist path of economic development.

Furthermore, there were additional factors. For political reasons, the great capitalist powers supported the feudal elements in the underdeveloped countries as an instrument for maintaining their economic and political influence. This provided another obstacle to the economic development of these countries. The repetition of the classical pattern of economic development in the underdeveloped countries, with a few exceptions, turned out to be impossible. As a result new patterns of economic development emerged.

What is the essential feature of the new patterns? I shall first describe briefly the socialist pattern of economic development which by now has crystallized into a pretty clear-cut form of economic organization. The socialist revolutions took place in countries which had a particular historic situation. They were underdeveloped, the classical capitalist pattern was not workable, though there was some industrialization on capitalist lines. A limited industrialization like that in Russia, produced an industrial working class and a political movement of the working class which became the chief agent of the social revolution.

The socialist revolution started everywhere with two acts. One was the nationalization of existing capitalist industry, trade, finance, transportation, and the creation on that basis of a socialist sector in the economy. The second act was an agrarian reform which abolished feudal social relations in agriculture, divided the land among the peasants, and at a later stage fostered cooperative development in agricultural production. These two acts provided the basis for the accumulation of resources for productive investment.

The nationalized industries—trade, finance, transport—provided a pool of profits which were used for additional industrial investments. As new industrial establishments were constructed, this pool of profits became larger. Again it was used for new investment, and thus the nationalized industrial sector of the economy grew by means of reinvestment of its own profits. In this way a process of self-sustained growth was started. However, these countries were underdeveloped and industry played a not very large role in their economies and was not sufficient to provide resources for the large-scale investment needed. An additional source of investment was a contribution of the peasants. The peasants, having received land in the agrarian reform, were made to contribute part of their proceeds by some form of taxation, mostly compulsory delivery of the produce at a lower price to the state. The revenue thus obtained was used for new investment. By reinvesting growing industrial profits and by investing the contribution of the agricultural population which benefited from the agrarian reform, a large accumulation was started. This made it possible to embark upon economic development, and this development then gradually became self-sustained and cumulative.

This is the essential feature of the socialist pattern of economic development. The third pattern, which I call the national revolutionary one, is only in the making and has not yet crystallized as clearly as the capitalist and the socialist patterns have. If you take the various countries which have emancipated themselves from colonial or semi-colonial dependence, you find rather large differences. Therefore, it may be somewhat more difficult to give a brief synthetic description of that pattern. Notwithstanding, certain general features are already apparent.

The general features of the national revolutionary pattern are the following. First, as in the socialist pattern, it is the state and public investment which is the most active, dynamic factor in economic development. The reason is simple. In the countries in question not enough of a capitalist middle class has developed to be capable of providing the capital resources for investment on a scale which is needed to achieve a break-through from the old stagnant into a developing economy. Therefore, public investment must become the leading factor of economic development, its very driving force. The second feature of the national revolutionary pattern is that it relies on nationalization in a different way from the socialist pattern. Nationalization of private capital plays a very prominent role in the socialist countries. In the national revolutionary countries nationalization is usually limited to foreign capital or certain parts of it. Very frequently the nationalization of foreign capital is not so much the result of an economic program, but of a political conflict with the old capitalist countries which makes nationalization necessary as a means of political emancipation and of asserting the independence of the formerly colonial or semi-colonial countries. Nationalization does not as a rule cover indigenous capital.

The situation in these countries is dominated by the struggle for national emancipation and the assertion of national independence. This creates a broad basis of national unity in which many capitalist groups participate and consequently take part in the national revolution. Furthermore, in many countries the amount of existing private capital, particularly in industry, is very small. There is not much to be nationalized, not much which through nationalization may contribute as a source of capital accumulation. Thus the national revolutionary pattern, while relying on public investment as the dynamic and guiding force of economic development, at the same time tries to mobilize whatever indigenous private capital exists and to encourage it to take part in the investment-serving economic development. It tries to channel private investment into productive activity.

In most of the national revolutionary countries a certain number of agrarian reforms take place. These reforms, among others, serve the objective of inducing the revenues coming from agriculture to be invested in industrial activity. Feudal landholding and use of land revenues for conspicuous consumption are removed; former landholders are encouraged to find their way into industrial investment.

Such is roughly the pattern of economic development which begins to emerge and which I have classified as the national revolutionary one. Both the socialist and the national revolutionary pattern have one feature in common. Economic development is not spontaneous as in the classical capitalist pattern but is consciously achieved through planning.

Economic planning was originally an invention of the socialist economy. But now it is gradually spreading throughout the whole world. Planning has been adopted as an instrument of economic development by national revolutionary countries, and the idea of planning even begins to enter the old capitalist economies. Thus the new patterns of economic development, which I have very briefly and very generally outlined in this lecture, also lead to the development of a new technique of economic development, namely of economic development through planning. Planning becomes the basic feature and instrument of economic development in our time.

Lecture II

PLANNING ECONOMIC DEVELOPMENT

Planning is a relatively new form of economic policy. It originated with the socialist economies and is an essential part of socialist economy. Under conditions where the major part of the means of production become publicly owned, it is only natural that the utilization of these means and the process of production be subject to a general national economic plan. However, planning as a method of promoting economic development has not remained limited to the socialist countries. It has spread first to the countries which follow what I call the national revolutionary pattern of economic development. In these countries it has become —in a similar way as in the socialist countries—the main instrument of promoting economic development. More recently the idea of planning is even spreading to the old capitalist countries as a part of the growing preoccupation with economic development.

As pointed out in my first lecture, in the capitalist countries the main preoccupation up to World War II was with problems of economic equilibrium; development was a spontaneous process and was not a subject of particular attention. But the rapid development of the socialist countries and the increasing importance of the problem of underdeveloped countries, which more and more adopt the national revolutionary pattern of economic progress, have created a challenge for the old capitalist countries. The challenge is twofold. First, not to lag behind the rapid rate of development of the socialist countries, to keep up in the international competition between the socialist and the capitalist economic systems, a competition which increasingly dominates the present world situation. Second, the need to find a solution for the problem of economic underdevelopment which has become a major issue in today's international politics. Thus the idea of planning reaches even the old capitalist countries. The fact that planning is connected with many international problems also raises the question of international cooperation in planning for economic development.

In the socialist countries and in the countries following a national revolutionary pattern we plan economic development, because economic development would not, under existing historic conditions, take place automatically. Consequently it must be planned.

What is the essential of planning economic development? I would say that the essential consists in assuring an amount of productive investment which is sufficient to provide for a rise of national income substantially in excess of the rise in population, so that per capita national income increases. The strategic factor is investment, or more precisely productive investment. Consequently the problem of development planning is one of assuring that there will be sufficient productive investment, and then of directing that productive investment into such channels as will provide for the most rapid growth of the productive power of the national economy.

These are the essential tasks of development planning. The problems which planning faces can be divided into two categories. One is the mobilization of resources for purposes of productive investment, the other is the direction of the investment into proper channels. These are the essential problems implied in planning.

The first problem is that of mobilizing resources for investment. Taking the experience of the socialist countries and of the countries following a national revolutionary pattern, a certain picture of methods employed for that mobilization of resources can be drawn. The two chief methods are: first—and this is the method which was paramountly applied in the socialist countries—nationalization of industries, finance, trade, and the use of the profits thus derived for purposes of investment. The other method, which particularly plays a role in the countries following the national revolutionary pattern, is nationalization of foreign owned natural resources and the use of the profits from these resources for investment purposes.

A further method is the contribution of the peasants in countries where agrarian reforms are carried out. The peasants are required, in return, to make some contribution to the state finances, which are used for purposes of investment. This frequently does not suffice and an appeal is made to resources derived from general taxation, public loans, and, in certain cases, also deficit financing.

These methods of raising resources for investment are applied both in socialist and national revolutionary countries in various proportions. There is also a method which plays a particularly important role in the national revolutionary countries, and which also played a role in certain socialist countries during a transition period. This is the inducement of private savers to undertake productive investment. This implies inducing private industrialists, traders, landowners, and financial groups, to invest a considerable part of their income in the direction that is conducive to assuring the country's rapid economic development, which means essentially investment in production. This can be achieved by various means such as, for instance, taxation of unproductive uses of wealth, compulsory saving, restriction on distributions of profits and on such uses of profits as do not consist of productive investment, compulsory loans, and all kinds of other measures. Finally, import of foreign capital may be also a source of financing productive investments. I shall not speak today of the latter source because tomorrow's lecture will deal with it in greater detail.

Thus there is a whole catalogue of means applied in various proportions in different countries which provide the resources necessary for substantial productive investment. By substantial productive investment I mean investment which is large enough to achieve a break-through, or as some economists call it—to produce the "take-off," the passage from stagnation to intensive development. This obviously cannot be done by small amounts of investment which are likely to peter out in a great number of minor projects. Sufficient investment is required to produce a real, a qualitative change, in the structure of the national economy.

The second problem is the direction of investment, and here I shall distinguish three sub-problems. The first is how to allocate investment so as to assure the most rapid growth of production; the second is how to secure balanced development of the economy, balance between the different branches of national economy; the third is how to assure efficiency in the use of resources in economic development, how to avoid waste of resources. These are three sub-problems of the general problem of directing investment so as to assure economic development.

The first sub-problem is the most important one. It is concerned with choosing such types of investment as will most rapidly increase the productive power of the economy. This implies a concentration of investment in fields which increase the capacity of further production; that means building up the industries which produce means of production. It is only through development of the industries which produce means of production that the production capacity of the economy can be raised.

This can be done, however, either directly or indirectly. It is done directly through investing in the construction of.

say, power plants, steel plants, machine industries, raw material production, and so on. It is done indirectly through foreign trade: instead of investing directly in the production, say, of certain machines it may be possible to get these machines from abroad by investing in the production of commodities which can be sold abroad in order to import the machines required. Thus the productive power of the economy can be increased either directly through investing in the production of means of production, or indirectly through developing export industries which make it possible to import in the future the needed means of production. Which of these two methods is used depends on all kinds of circumstances, on existing facilities for developing either directly the output of means of production, or for producing commodities for export. However, if investment in exportable commodities is undertaken, then obviously it must be associated with importation, in exchange for these exports, of machinery, steel, and other means of production to increase the country's productive power.

However, investment in the production of means of production is not the only type of investment needed. There are two complementary types of investment which are necessary. One is investment in agriculture to increase food production. The experience of economic planning, particularly in the socialist countries, has shown that with the growth of industrialization, with an increasing part of the population being employed in industries or transport services and so on, a considerable surplus of agricultural products is needed to feed the non-agricultural population. Consequently, complementary to investment in the development of the output of means of production must be investment in agriculture to increase agricultural output. Also a certain amount of investment in industries producing consumer goods for the population is required, for the standard of living rises with the expansion of industrial employment and output. These are then the chief directions of developmental investments. The first one is the strategic one, the one which brings about economic development, and the other two are of a complementary nature necessary in order that economic development can proceed smoothly.

Finally, there is one important field of developmental investment, namely investment in the general economic infrastructure of the country, such as transport facilities, roads, and also social services. These, too, are complementary investments needed to assure smooth economic development. However, by themselves they are not a factor bringing about development. One of the problems in many, if not most, underdeveloped countries was—and this was a part of the colonial or imperialist system—that there took place a large investment in this economic infrastructure purely for the needs of colonial exploitation, and not for development of the productive power of the country.

In choosing various allocations of investment, or rather the right proportions between various allocations of investment, the problem of the choice of technology arises, the question whether to use labor or capital intensive methods of production. Very frequently, it is argued that since in underdeveloped countries there exists a large supply of unemployed or underemployed labor power, the most labor intensive methods should be chosen so as to secure a rapid increase of employment.

Usually the situation is such that there is a distinction between the methods of production which employ much labor and those which are more productive in the sense of contributing more to the increase of net output of the economy, i.e. of national income. Thus there emerges a dilemma in underdeveloped countries whether to use methods which are less labor intensive, provide less employment, but rapidly increase output and national income, or whether to choose methods which are labor intensive but which lead to a slower rate of increase of output and national income. The decision to be made depends on the period for which you plan. If planning is made only for a short period, then one might argue that the most labor intensive method is the best because it leads most rapidly to the absorption of unemployment or underemployment.

However, if you take a longer view of development, then you find the following. By investing in methods, as well as in industries, which yield a rapid increase of output, you get a more rapid increase in national income. If a certain proportion of national income, for instance 20 percent, is invested, it turns out that by choosing the method and allocation of investment which increases national income more rapidly, even if it is less labor intensive, after a number of years national income will have grown to such an extent that the total amount of investment will become sufficiently large to provide more employment. On the other hand, a more labor intensive method would have led to a slower growth of national income, and consequently also to a slower increase in the absolute amount of investment. Thus after a certain period it always pays—also from the point of view of employment—to use that method and that allocation of investment which contributes most to the increase in national income, i.e. the net product of society.

This is the basic principle to be observed in a plan which aims at a rapid increase in the productive power of the economy. It may be that a certain amount of unemployed labor can be employed "on the side" in ways which use very few capital resources, and thus can be called upon to make some contribution to the increase in production and consequently to national income. This is being done very successfully in China. But still this is, so to speak, a secondary line of activity. The strategic activity in securing rapid development must consist of such methods of production and such allocation of investments as will most rapidly contribute to an increase in net output. In the long run, this proves to be the way which provides more employment than the alternative method of starting with labor intensive but less productive investments simply in order to diminish underemployment.

In planning economic development, the problem of foreign trade usually turns up as a major difficulty. The development of industry in any less developed country requires in the initial stage a considerable increase in imports of machinery, steel, and other means of production. For in the very beginning stage of economic development these cannot be produced at home; this immediately puts a burden on the balance of payments. In the second stage, when the basic industries which create the country's productive potential are already constructed and start producing, there arises a requirement for increased imports of various raw materials and also of further imports of machinery to continue the process of industrialization. The process of industrialization, in turn, requires increased imports.

There are certain countries which are in a particularly fortunate position, since they have large exportable resources providing considerable revenues in foreign exchange. Before embarking on planned development, these revenues usually were not used, or were used only to a small extent for productive investment. Now they can be used for that purpose. To cite examples: in Iraq export of oil provides such a resource, in Ceylon the export of rubber and tea. There are such resources in the United Arab Republic, for example cotton; I would also classify as such an exportable resource the Suez Canal. Countries which are in such a fortunate position have immediately available a certain amount of foreign exchange with which they can import machines and other commodities necessary for industrial development.

Countries where such exportable resources do not exist or exist in small quantities have to go through a period of austerity, cutting down imports of consumer goods, particularly luxury goods, in order to free the exchange necessary to import producer goods and raw materials. Very frequently, it is exactly this necessity to impose a high degree of austerity on the consumption of imported goods. which limits the possibility of rapid economic development. Here, of course, the situation can be aided by foreign capital, foreign loans, but this is a subject which I want to deal with in tomorrow's lecture. These are roughly the directions of investment required to assure economic development. These investments, however, must be coordinated; balancing investment and production in the different branches of national economy is another important aspect of planning.

There are two kinds of balances which must be secured: one is physical balance and the other is financial or monetary balance. The physical balance consists in a proper evaluation of the relations between investment and output. In the countries which already have experience in economic planning, investment coefficients are computed. These coefficients indicate the amount of investment, and also the composition of that investment, in terms of various kinds of goods needed to obtain an increase of output of a product by a given amount. For example, how much iron, how much coal, how much electric power is needed in order to produce an additional ton of steel? On this basis the planned increase in output of various products is balanced with the amounts and types of investment. It is also necessary to balance the outputs of the various sections of the economy because, as we know, the output of one branch of the economy serves as input for producing the output of another branch. For instance, the output of iron ore serves as an input in the steel industry. In the last mentioned field, a special technique, that of input-output analysis, has been developed.

The physical balancing mentioned is necessary in order that the output of the different branches of the economy proceed smoothly. This is a condition for the internal consistency of the plan. If this condition is not observed, bottlenecks appear. The plan cannot be carried out because of physical obstacles, such as lack of raw materials, of man-power, etc.

The second kind of balancing is monetary balancing, assuring monetary equilibrium in the economy. This consists in establishing an equilibrium between the incomes of the population—wages, incomes of peasants and others—and the amount of consumer goods which will be available to the population. If the amount of incomes, or more precisely that part of the incomes which is spent for purposes of consumption, should turn out greater than the amount of available consumer goods, inflationary processes develop. Thus the financial or monetary balance must establish an equilibrium between the part of incomes devoted to consumption and the output of consumer goods. Further it must establish equilibrium between the part of incomes of the population which will be used for private investment and the amount of investment goods made available to private investors. Finally, in the public sector a balance must be established between the financial funds made available for investment purposes and the amount of investment goods which will be produced or imported. In addition to these balances, it is necessary to establish the balance of foreign payments and receipts. The financial balances are an important part of planning. Just as the lack of physical balance leads to physical obstacles to the smooth process of production, so the lack of financial balance leads to disturbances in the supply and demand for physical commodities, and finally also to physical disturbances in the process of production.

Looking back upon the experience of the countries which have applied planning as a tool of economic development, I must say that it has usually turned out to be difficult to maintain the proper financial balances. Few of these countries escaped inflationary processes during certain periods. These processes were due to the wage bill rising more rapidly than the output of consumer goods. However, in theory and with the experience which has been gained in earlier years, it is today quite possible to plan the financial equilibrium of economic development in a way which avoids inflationary processes.

A last point—to be mentioned only briefly—is that of securing efficiency in the use of resources in the process of economic development. This is connected with the use of the price system. The function of the price system in economic planning is twofold. Prices serve as means of accounting, namely as a means of evaluating cost of production, value of output, and comparing the two. For this purpose it is necessary to have a proper price system which reflects the social cost (and, in the short run, the scarcity) of the various means of production and the social importance of the various products. Without such a price system, cost accounting would not have any objective economic significance. This is one role of the price system; the other role is that of an incentive.

The plan of economic development has two aspects: in the public sector it is a directive to various public agencies and enterprises to do certain things, e.g. to invest so much in such a way, to produce by such methods at such a cost. With regard to the private sector, the plan lacks the power of a directive, but is a desire expressed which must be followed up by creating incentives that will induce private producers to do exactly the things which are required from them in the plan. It is quite clear and does not require further explanation that with regard to the private sector the price system, including interest rates, is an important incentive serving to induce the private sector to do the things required from it in the plan. But also in the public sector the need for incentives exists. It is not sufficient just to address administrative directives to public agencies and public enterprises. In addition, it is necessary to create economic incentives so that the public agencies, enterprises, etc., find it in the interest of their managements and their employees to do the things which are required from them in the plan. This again requires a proper price system.

Thus the price system plays, in planning, a role both as a basis of accounting and as an incentive inducing the people to do the things required from them in the plan. A certain general observation may be made here. It seems to have been a rather general historical experience that in the first phase of economic development, particularly of industrialization, the problem of a proper price system is not the most important one. In both the socialist and the national revolutionary types of economic development we find that in the first period the main problem is not that of the details of accounting or incentives. The main problem is assuring rapid growth of productive capacity. The question of rapidity of growth overshadows the more subtle questions of high-grade efficiency. It is more important, for instance, to develop the machine industry than to do it in the most efficient manner. Too much preoccupation with the subtleties of economic accounting may hold up action and slow down progress. It is only at a higher stage of economic development, when the national economy has become more complex and diversified, that the problem of efficiency and incentives becomes increasingly important. It is then that the subtleties of assuring the highest efficiency through proper cost accounting, properly established incentives, etc., come into play.

Thus, though I do not want to minimize the importance of the problem, I do believe that it is not the most important problem in the first stage of economic development. In this first stage, the take-off stage, the real issue is to mobilize the necessary resources for productive investment, to allocate them to the branches of the economy which most rapidly increase the productive potential of the country, and to do so by the most productive technological methods. At a later stage, more subtle aspects of planning come into play. Thus a certain crudeness of planning in the early stages of economic development is, I believe, quite justified.

Lecture III

ECONOMIC DEVELOPMENT AND INTERNATIONAL COOPERATION

I intend to speak this evening of international cooperation and economic development. The problem of international cooperation acquires today new and important features. This is due to the coexistence in the present world economy of the three patterns of economic development of which I have spoken. It is the coexistence of countries with a capitalist system, countries with a socialist system, and countries which follow what I call the national revolutionary pattern of development. The coexistence and at the same time competition of the capitalist and socialist systems, on one side, the question of economic underdevelopment and of national revolutions with their economic consequences, on the other side, pose new problems to the world economy.

The problems are essentially three. One is the problem of international trade under conditions where there are various economic systems and patterns of development in world economy. The second is the problem of aid, and it is usually formulated in terms of aid to the underdeveloped countries which have undergone or are undergoing national revolutions. The third problem is political in origin, but has important economic consequences, namely the problem of disarmament.

It is this last problem which I shall consider first. I shall consider it first because disarmament has become the paramount political problem of our day and because its economic consequences will have important repercussions on international trade and also on the problem of action on behalf of underdeveloped countries. I do not intend to discuss here the political aspect of the problem of disarmament. With the destructive power of modern weapons, the problem of disarmament has become a problem of life and death for the human race; I think it is sufficient to mention this insofar as its political aspect goes. But there are economic problems involved in disarmament. These problems have a different aspect in socialist and in capitalist economies.

Radical and rapid disarmament undoubtedly creates certain economic problems in a socialist economy. The problems are those of reallocation of large resources—industrial plants, equipment, raw materials, and also human manpower—from production for armament to production for non-military purposes. Obviously, when such reallocation is to take place rapidly on a large scale, there arise certain problems of readjustment, of new directions of production, of transfer of manpower, of organization of economic activities. In a socialist economy these problems are largely problems of proper planning and management of the national economy. The difficulties are of a character which economists usually denote by the word frictions. There are all kinds of frictional obstacles involved in the transfer of manpower and reallocation of resources. With proper planning, however, and proper managerial skill, they can be overcome.

The problems are more complicated in the capitalist economy. There, too, frictional difficulties arise. But in addition a special type of problem arises which is peculiar to the mechanism of the capitalist economy. This is the question of effective demand. A large-scale and rapid reduction of expenditures for armaments reduces the demand for the products of armament industries. These reduce their output and employment, and this leads to a reduction of effective demand by the population. This tends to result in a further reduction of demand for consumer goods and for investment goods. This, in turn, leads to further reductions in output and employment. The process may become cumulative, causing a recession or even a depression and, consequently, mass unemployment. Therefore we find in the leading capitalist countries, particularly in the U.S., serious apprehension concerning the economic consequences of disarmament. Frequently we observe that whenever the political situation becomes favorable to prospects of disarmament, quotations on the stock exchange begin to fall.

This, however, does not imply that it is definitely impossible for the capitalist countries to carry out disarmament without running into recession or even depression. It only implies that under conditions of capitalist economy, disarmament must be accompanied by certain measures of economic policy which are designed to counterbalance, to compensate the falling off of effective demand and to prevent it from generating a cumulative reduction of economic activity. This is possible by means of internal measures activating investment, public or private, and also by certain measures in the field of international economic cooperation. It is about the last mentioned measures that I want to speak.

One such measure is an increase in international trade, another is planned action to aid the economic progress of underdeveloped countries. I believe that measures of economic policy in these two fields can compensate in the capitalist economies for the decline of effective demand caused by disarmament; moreover, they can even overcompensate it, and create new conditions for economic development. At the same time, disarmament in the leading capitalist and socialist countries can free important resources which can be utilized in an international program of economic development of the less developed areas of the world. Various proposals have been made to use part of the financial and physical resources saved by disarmament to promote economic development in those areas of the world which most need such development. Consequently, consideration of the economic implications of disarmament leads us to the problem of international trade and to the problem of planned aid to underdeveloped countries.

Let us consider the question of international trade. After World War II, international trade suffered very much because of the Cold War. The Cold War, for a certain period, has greatly reduced, and in certain cases almost stopped, trade between capitalist and socialist countries. It has also affected very strongly the foreign trade possibilities of the underdeveloped countries in Asia, Africa, and Latin America. For the trade connections of these countries have been subjected, or at least attempts have been made to subject them, to considerations of Cold War policies imposed by the great capitalist powers. In the last few years the international political atmosphere has improved, there has been considerable relaxation of international tension, and many of the underdeveloped countries have emancipated themselves from the influence of Cold War pressure. The emancipated countries have used their newly won freedom in economic policy to develop trade relations not only with capitalist but also with socialist countries, thus extending their area of choice of trade partners and so gaining a better position in international trade relations.

But we still are far from having exhausted the opportunities of expanding international trade. In Europe, for instance, the trade between the countries of Eastern and Western Europe, though it has increased in the last years, is far below the potential possibilities. The situation is even worse in Asia where many countries are still prevented from maintaining normal trade relationships with socialist countries, particularly with China. Consider the absence of any significant trade between Japan and China, which, from the point of view of economic geography, is sheer nonsense. The development of foreign trade relations unhampered by considerations of the Cold War can provide for all partners concerned great opportunities of economic progress.

The most important factor in this field is the rapid development of the socialist economies. It may suffice to say that the present five-year plans of the socialist countries imply that by 1965 approximately half of the world's industrial output will be produced in the socialist countries. As socialist countries comprise 35 percent of the world's population, this means that per capita output in the socialist countries will by 1965 be higher than in the rest of the world, though not higher than in the most highly developed countries of Western Europe and the U.S.

Of the whole population of the world, 19 percent live in the developed capitalist countries, 35 percent live in the socialist countries, and 46 percent live in countries which were until recently dependent on the leading capitalist countries and now are in various stages of their process of emancipation or of struggle for emancipation. Given this situation, it is obvious that the socialist countries will increasingly provide a market for exports as well as a source of supplies, particularly in the field of industrial products. Thus if we manage to remove the restrictions on international trade which have been built up during the Cold War, we may look forward to a quite important increase in international trade.

This is particularly important for the underdeveloped countries, especially for countries which are exporters of raw materials and in whose economic life the exports of raw materials play an important part. These countries have suffered in the last few years very heavily from a fall in prices of raw materials. Thus in the period from 1953 to 1958 raw material prices fell by 7 percent, while industrial prices rose by 4 percent. In the two years of the last economic recession in the leading capitalist countries, 1957 and 1958, the raw material exporting countries lost, in consequence of the fall of their export prices, $2 billion each year. This shows the importance of foreign trade conditions for the underdeveloped countries. It turns out that during the years 1957 and 1958 the loss suffered by these countries due to the fall of prices of the raw materials exported was equal to the amount of loans obtained from the International Bank for Reconstruction and Development over the last 6 years. The loss due to the fall in export prices probably counterbalanced, and maybe even surpassed, the amount of foreign loans the underdeveloped countries received. Thus regularization and expansion of foreign trade is essential to the economic progress of the underdeveloped parts of the world.

This, however, is not sufficient. In addition, the underdeveloped countries need capital from the more advanced countries. Speaking of the need of foreign capital for the underdeveloped countries, it must be clearly realized that economic development of these countries cannot be based on foreign aid. It must be based on the mobilization of internal resources. If we really want to develop all that part of the world in which 46 percent of humanity live, then the capital resources which both the leading capitalist countries and the leading socialist countries can put at the disposal of such a development are insufficient. Therefore, the internal effort of capital accumulation must be the basis of economic development. However, foreign capital may play an important auxiliary role, facilitating the situation particularly in the so-called take-off period, and even in the early period of self-sustained development. It is just in such an early stage of development that machinery and raw materials are needed, while the industries are not yet ready to provide sufficient products for export purposes. In such a transitional period, foreign capital aid may be of great and even crucial importance.

With regard to foreign capital, we have to face one very important fact. This is the decline in the role of private international capital movements. This decline is of structural and permanent character. It is the result of the very process of emancipation of the former colonial or otherwise dependent countries, of their embarking upon the national revolutionary road of development. Under these historic conditions, the requirements of private capital ready to be invested in such countries, and the requirements of these countries as to what they expect from foreign investment are very different and not easy to reconcile.

In the imperialist period, the period that started with the last quarter of the 19th century, private capital investment in underdeveloped countries did not follow the classical pattern which is described in the old economics textbooks. It was investment of monopoly capital reaping exceedingly high profits, not due to its economic contribution but through political domination over the country in which the investment was made. Political domination provided the monopoly privileges and possibilities of excluding competition of capital from other countries. This also led to the consequence that foreign capital investment was largely of a peculiar colonial type and did not set in motion a process of development of the economy of the dependent countries.

With the progress of the movement for emancipation from colonial and imperialist domination, these terms of investment became impossible. What was a very important inducement to investment in the less developed countries—the particular privileges foreign capital enjoyed—disappeared. In addition, another problem emerged, namely, the problem of safety of the foreign investment, safety of private foreign capital. This problem of safety had arisen by the early period of capital exports in the 19th century. At that time it was a question of protecting investment from the capitalist countries in the less developed countries against arbitrary expropriation and restrictions imposed by precapitalist governments of a feudal or even more primitive type. The desire to assure the safety of investment became a powerful force behind colonial expansion, behind establishing colonial or other forms of domination in the countries where precapitalist conditions prevailed.

Later, there came a period when international private investments flourished. These investments, however, increasingly became monopolistic in character. At present a new concern about the safety of private investments arises: the concern about their safety from nationalization. Financial circles in the leading capitalist countries, when asked about investment in the underdeveloped areas of the world, always put the question of guarantees—guarantees first of all against nationalization. Here the basic conflict between the requirements of private investors from the leading capitalist countries and of the countries entering upon national revolutionary development becomes apparent.

Of course, certain guarantees can be given by national revolutionary governments to various foreign capitalist groups. Such guarantees, however, must of necessity be restricted to certain groups and limited in scope. For the national revolutionary governments cannot give guarantees which would prevent the national revolutionary states from exercising their sovereignty in determining their own pattern of economic development. The requirements of economic development of the national revolutionary countries differ from the interests of foreign capital investors. This fact is crucial in the historic period in which we live, and it puts a limitation on the possibilities of developing international private capital movements to the underdeveloped countries on a large scale. Such movements are not entirely impossible, but their role is limited and on the decline. They can no longer play the historic role of an important factor in economic development. Their significance becomes of secondary or even tertiary importance.

One aspect of international private investments deserves particular attention. The classical type of foreign investment by the leading capitalist countries was direct investment. But precisely for reasons of maintaining and asserting their national sovereignty, the new independent countries want loans rather than direct investments. This factor limits very strongly the future of private capital investments.

The international investments which increasingly dominate the scene in the present period are of two types. One is investment based on bilateral agreements between state and state. This type of investment is today adopted by the socialist countries in their relations with the countries following the national revolutionary pattern of development, as, for instance in the case of the Soviet Union and the United Arab Republic in constructing the Aswan High Dam. The same type of investment rises in importance even in relations between capitalist countries and the national revolutionary countries. A relation of state to state or sometimes a relation of private capitalist in the capitalist countries to the state in the national revolutionary countries occurs today with increasing frequency.

The type of investment mentioned increasingly replaces in importance the private capital investments of the classical type. Direct investments of private capitalists in the less developed countries cede their place to loans by private capitalists or by the state to the newly independent states. In the field of international investments an important development has taken place. This development is the result of the entrance of the socialist countries, in particular of the Soviet Union, the largest of them, into the field of aid to countries developing according to a national revolutionary pattern. The aid of the Soviet Union and of other socialist countries has already influenced, and will increasingly influence, the types of investment made by the capitalist countries in the countries following the national revolutionary pattern of development.

This has become quite clear, for instance, in the case of India; also the United Arab Republic may serve as an example. The active role of the socialist countries, particularly of the Soviet Union, in promoting capital aid to the national revolutionary countries has caused a change in the investment policy of the leading capitalist states and of the leading private capitalist groups. It has forced these states and groups to abandon to a certain extent the old type of colonial investments, and to adopt types of investment which are directly conducive to the development of the industrial potential of the new countries. In the case of India, the policy of the leading capitalist groups in Great Britain was rather adverse to fostering industrial development and particularly the development of heavy industries. But the moment the Indian state started to develop a steel industry with investment aid from the Soviet Union, British capitalists were quite ready to come in and provide a loan for the development of the Indian steel industry.

The foreign aid policy of the socialist countries has forced capitalist countries and private capitalist monopolies to revise their investment policy in a way beneficial to the development of the national revolutionary countries. This process is only in the beginning: it works already in India and in the United Arab Republic; but it still does not work in many other underdeveloped countries. I am sure, however, that we are seeing the beginning of this process, and the greater the activity of other socialist countries and of the Soviet Union in this field, the more the leading capitalist groups and their governments will have to revise their investment policies. There arises, however, the problem of coordination of such international investment activities, and in particular the problem of an international program of development for those areas in the world economy which are still heavily underdeveloped. Such a coordinated international investment program would have to be undertaken by, or at least under the auspices of, international organizations.

For quite some time, the countries of Asia, Africa, and Latin America have been demanding that the United Nations set up an agency to finance development projects in these countries. Certain steps have been taken in this field by the United Nations, though they are of a very limited character. But should disarmament really be carried out on a large scale, some part of the resources thus saved in the budgets of various countries might be used for purposes of international economic development. If this happens, the question of international investment projects financed by international agencies will become of increasing importance. Thus we may look forward toward a future where important international economic development is financed by funds provided through international agencies. That means, of course, through agencies in one way or another under the auspices of the United Nations. However, though it seems to me that such a prospect is clearly on the horizon, I think that the situation at the moment is not yet ripe for it. The latest experience of the United Nations action in the Congo has shown that the United Nations executive organs are not yet a truly international body. They are used to reassert colonial or neo-colonial policies. In the long run, the United Nations undoubtedly will play an increasing role in the planning and financing of international economic development. But at the moment the United Nations executive machine is still too much under the influence of imperialist and colonial powers to be suitable for such a task. Notwithstanding, the process of maturing of the United Nations Organization will proceed. With the increase of the economic and political significance of the struggle for colonial emancipation and of national revolutionary countries, together with the further growth of the economic potential and of the political significance of the socialist countries, the United Nations will gradually mature to perform this new task.

We can look forward to the United Nations becoming a truly international agency which will no longer be capable of being used for purposes of reasserting colonial or semi-colonial policies, as unfortunately was the case recently. Then the United Nations will be able to play its role as an instrument of international economic cooperation and international planning and financing economic development.

International cooperation for economic development is not limited to action in the underdeveloped areas of the world. Even the most developed countries in the world could benefit from such action. Countries like the United States and the Soviet Union which today are the leading industrial powers of the world can also undertake common projects of economic development. Actually, various scientists have already proposed such projects, as for instance connecting the United States, the Soviet Union, and Western Europe by railway through Alaska and the Asian and European continents.

I do not want to evaluate the technical or economic feasibility of such projects. I just mention them to show that even the most developed industrial countries can find a useful field of commonly planned economic cooperation. There is also the possibility of economic cooperation in the field of scientific and technical research which will rise in importance. Already we have reached a situation where certain fields of scientific and technical research, like the utilization of atomic power or the conquest of space, are not accessible to smaller countries simply because they do not have sufficient economic resources for such research.

The time will come when even the largest countries will not be able to afford the expenses in certain fields of scientific and technical research and will have to pool their resources. But already at the present stage smaller countries which are interested in cooperation in the scientific and technical field may pool their resources. In particular, countries which follow the national revolutionary pattern of development may wish to pool resources on a regional basis.

This brings me to the question of cooperative regional arrangements for economic development. Such regional arrangements may play an important role—regional arrangements by which certain countries pool their resources to provide for economic development. Cooperation on a broader geographical scale depends on the political situation; it requires relaxation of international tension and peaceful coexistence between countries following different patterns of development. Such coexistence opens great possibilities for concerted action in the field of economic development.

One thing, however, has to be made clear, namely, what peaceful coexistence and cooperation can mean and what it cannot mean. It can mean all that I have said about pooling resources for international development plans to the benefit of all the partners concerned. It cannot mean a stoppage of processes of social progress and social change. International cooperation is not possible on the terms that the struggle for emancipation from colonial rule should be stopped, and that nations which have not yet gained their independence should give up their aspirations and objectives. Neither is international cooperation possible on the terms that social changes do not take place in countries where they are mature, where the economic and social structure requires them and the population wants them. Economic cooperation cannot imply a freezing of the status quo of imperialist, colonial domination or of antiquated economic and social systems.

To expect that would be unrealistic; we must face the realities of the situation. Peaceful coexistence and international cooperation, however, can mean that changes which become necessary and cannot be prevented take place through peaceful means and in a way which does not make them a cause of increase of international tension, and in particular a cause of war. This is what we realistically can hope for: a situation whereby means of international cooperation, necessary political and economic adjustments, national emancipation, and economic and social progress are achieved in a peaceful way. To be workable, it must be a situation in which progress continues, and in which the people of the world improve their economic, social, and cultural situation. This is the type of international cooperation we all can look forward to realistically, cooperation which we can expect and which certainly is worth striving for.

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