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COMPREHENSIVE PLANNING AND COMPREHENSIVE  
EXTERNAL UNCERTAINTY

SOME PROBLEMS OF NATIONAL DEVELOPMENT PLANNING AND  
FOREIGN FINANCING

(Based on the Notes for a Lecture to the  
Economic Society by Dr. Reginald Herbold  
Green, January 6th, 1967)\*

A national development plan is - or should be - a form of budget. This has a number of implications for plan formulation and implementation and - of particular interest in the present context - for the relationship between comprehensive planning and foreign financing.

A budget sets out to achieve certain aims, by using a limited supply of resources in a specified manner. Two characteristics are that a budget should cover a stated time period and that its resources, their specific uses, and the targets representing the aims should be in quantitative form. In no sense does this imply that the aims of a comprehensive development plan are purely (or even basically) economic nor that they are inherently quantitative. Realistically ultimate national goals are not basically economic but socio-political. So long as they are selected in the national interest and with careful consideration of the cost of achieving any one objective in terms of other objectives foregone because of resource allocation to the first objective, it is eminently proper that national resources should be allocated to achieve "non-economic" goals.

However, it does not follow that economic considerations are minor. The attainment of any objective cost resources - the efficient allocation of scarce resources among competing goals is at the heart of economic analysis. The aim of a better life for the majority of the population is basically social but it requires a rise in consumer goods and services supplies available to the population and a rate of increase in these supplies faster than that of population.

To sustain such an increase requires a growth of national output, of investment, of public services of an investment nature - e.g. technical education, road maintenance, agricultural extension. Other services of a consumption nature - e.g. pure water, museums, cultural programmes - represent public consumption for private welfare and therefore require resource allocation via taxation for their support. Thus the allocation of resources in such a way as to attain and maintain a rapid rate of growth in domestic output per person (that is if resources available) is essential for the efficient pursuit of national socio-political goals. Economic advance alone is not developed but without economic advance national

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\*The views expressed are the responsibility of the author and do not necessarily express the opinions of the Tanzania Treasury.

development, at least in a poor (low resources available per person) economy such as Tanzania's cannot be maintained for long.

A comprehensive development plan therefore sets out its aims in the form of quantitative targets (of total domestic product, of exports, of school enrolments, of water supply points, etc) to be attained by the use of policy and project instruments which either direct or influence the allocation of resources. To be useful a plan must be possible, that is the use of the available resources through viable project and operational policy instruments must be capable of achieving the stated targets. Further, it must be consistent, that is the inter-relationships of supplies and demands must be such that anomalies, e.g. completed schools without teachers or new factories with no foreign exchange to pay for raw materials, are avoided.

Finally, it must be reasonably efficient. That is the size of the targets in relationship to each other and the choices among alternative policies and projects as means toward achieving them must be such as to achieve a more rapid rate of national development (as defined by national decision makers on behalf of and, hopefully in response to popular needs and aspirations) than would a different choice of targets, policies, and projects. This is analogous to the evident fact that in personal budgeting one can increase or decrease welfare by laying out ones funds for different selections of goods (e.g. a lower cost radio and a better selection of food as opposed to a higher cost radio and very meagre food), by using alternative methods of doing something (e.g. taking a bus as opposed to a taxi and then having more funds for beer or dinner or postal savings) or by finding the same good at a lower price.

Planning in development economics has become more and more instrument and efficiency conscious in recent years but largely in relation to projects and their viability. Clearly this is an advance - unsound projects in the public and parastatal sector waste scarce resources and often hinder private sector activity. A money loosing national airline, for example, dissipates potential public investible surplus, reduces foreign exchange available for capital goods imports, and reduces the expansion of road and ocean transport needed for agricultural and industrial growth. A high cost public petroleum refinery raises the costs of all fuel using industries - e.g. transport, manufacturing - and thus raises their prices to consumers, lowers their competitiveness with imports, and acts as a brake on their expansion.

Policies, however, are at least as critical as projects. In relation to inducing private sector allocation - by farmers, by consumers, by small firms, as well as by large investors - public policies are often more critical than public projects.

The same holds for parastatal and other publicly owned but separately managed bodies and for co-operatives. It is, for example, no use to provide electric power for industry and follow a price policy making its use un-economic or to build roads through a potential cotton growing area while pursuing cotton price policies deterring farmers or failing to pursue extension - pesticide - fertilizer - seed policies assisting farmer initiatives.

## II

Foreign resource procurement and use pose a number of very critical policy questions. Wrong decisions on these can be extremely costly in terms of plan efficiency or even continued possibility. All too often the wrong decisions have been taken, not it should be underlined simply by developing economy politicians but also by their economic civil servants and advisors and by the governments of the industrial aid transferring states.

Use of contractor finance, approaches to reconciling external financial source preferences with national plans, and the use of closed or more competitive contract negotiations involve policy decisions whose result can not only increase or reduce the effective value of the foreign resources procured by very large percentages but also greatly alter plan focus, administrative and economic efficiency, and standards of political, public, and business honesty.

Contractor finance - whether from private Western firms often backed by state export promotion guarantees or from Socialist state expert monopolies - almost always entails very high direct and indirect costs. Repayment is usually in installments - often beginning before the contracted unit is completed - over less than ten years so that the effective period of the full loan is often less than four years following the initial use of the project purchased. On Western contractor finance the effective interest rate is usually over 10% and often over 20% - on Western and Socialist alike the actual plant cost tends to be well above competitive levels. Early repayment makes it impossible to pay for the productive unit out of its own earnings. In practice steadily rising levels of contractor finance (and associated costs) become necessary to repay the initially borrowings let alone to keep investment rising.

A series of West African states - of very different political and economic system and outlooks - have opted for heavy use of contractor finance, in at least two cases with disastrous results to the extent of piling up total contractor debts far in excess of annual export earnings. In at least one instance senior economists advised this policy on the grounds that manufacturing investment

raises exports or reduces imports rapidly enough to allow self financing of repayments and that in eight years the whole structure of production and balance of payments position could be transformed. This involved serious underestimation of the lag between initial ground breaking capacity operation as well as of the growth of repayment demands and serious over-estimation of net import substitution and export growth. As in the case of other states, massive finance was initially obtained - dominantly from Western firms backed by government export guarantees whose basis effects were to encourage unsound investment and finance policies, guarantee private profits, and encourage dealings with high cost (and in several cases palpably dishonest) firms all in the sacrosanct names of "foreign aid" and "export promotion." Soon debts could only be repaid and new projects instituted if new contractor finance per annum exceeded 30% of export earnings - a situation deterring any long term lender and leading to a panic by the short term lenders as soon as the flow of new borrowings began to fall. The economists (who indeed changed their views on contractor finance before the crash but still too late to avert it), the selling firms (who by and large have their profits), the government export promotion bodies (who after all promoted exports and presently piously protested at claims of inability to repay on time) are not greatly hurt. The government and development plan, however, have vanished without a trace and the economy is now faced with a very substantial foreign debt and a new investment policy as overcautious as the old was overcredulous. Capital area unemployment has "boomed" from 10% in 1965 toward 35-50% today.

Contractor finance has uses - as a limited supplement to basic sources of foreign finance. If - as in a few cases in Tanzania - a particular project or building is critical to the effectiveness of much broader investment, administration, and production operations, then a very high price whether in terms of interest or stated price may be worthwhile. The point is to evaluate costs, repayment schedules, and future financial implications clearly and to recognize that to borrow short at high cost to finance long term investment is unsound except as a method of filling minor gaps in a financing programme basically tied to long term resource procurement.

Foreign aid and loan sources - public and private, bilateral and international - have their own views on what projects and programmes developing economies should undertake. Their reasons are mixed - economic interest, political strategy or preference, drawing analogies from their own economic history, disinterested technical and economic appraisal. Some of these reasons are at least partially legitimate, all are facts of world economic life, all pose problems for development plan financing and implementation.

Three methods of "reconciling" aid donor interests and plan goals have proven crippling to national economic development. The first is to secure a major donor's experts to write the plan (as a number of African countries have) with the predictable result that its overall aims are automatically suspect (not always correctly), its national support low, but its external financing at least substantially assured. All too clearly neither national economic nor political development can be expected on this path whether the plan draft is a country, an international institution, or a consortium. A national plan can only be drawn up by experts responsible solely to national leadership.

Second, national plans can - in fact if not in name - be submitted to a limited number of aid sources for their re-drafting over overtly or projects to be financed selection. The plan then proceeds on the basis of the financed group which may bear a good deal of relation to perceived aid source interests and much less to initial developing economy goals. The belief that relationships between EEC and certain of its member states on the one hand, and many EEC African associate economies on the other, have been of this nature underlies the central criticisms directed at pattern of 6-18 relationships. One author put it (perhaps a trifle too harshly) - economic policies and plans may now be proposed in the African capitals but they are still disposed in Paris and Brussels with very little real influence by the Associate on the crucial financing decisions.

Finally, national plans can be amended in the course of implementation to take account of foreign financing preferences and availabilities. This course of action is not necessarily unsound. Many possible changes do not compromise basic plan aims, a certain number of overseas proposals for alterations are likely to be potentially consistent, or at least compatible, with national development aspirations.

The danger - especially if the contractor finance element is high - is that alterations on an ad hoc basis will be made without reference to their impact on overall plan objectives and resource allocation patterns. The result is likely to be one of very inconsistent plan fulfillment, e.g. 150% in civil service offices and housing, 150% on main roads and bridges, 25% on directly productive investment at the halfway point in one major plan. As the illustration suggests, ad hoc alterations are peculiarly likely to allow or provide cover for fraud. In the state in question an issue by issue approach to such policies as tariffs and project by project handling of development were in fact the facade for a political system whose philosophy was that the proper purpose of

holding responsible public political office was the promotion of personal, family, and local interests through the misallocation of public funds. That government too is no longer with us, its heritage of violence, chaos, and national agony will be long in abating.

What is needed is a clear set of priorities in the context of which really key projects can be pushed ahead purely on domestic resources when foreign are not forthcoming while alternative coherent sets of desirable but individually less essential projects can be built up to take account of the specific nature of foreign finance available. As Tanzania's 1964-1966 experience suggests, such an approach is complex and demanding at the implementing ministry, development planning, and treasury levels but is also workable and, hopefully, perfectible. It is especially important for an economy seeking to diversify its sources of foreign finance to broaden the range of programmes for which finance is available, lessen its concentration of economic dependence on a handful of much longer economies, and - in general - increase its overall international economic freedom of manoeuvre and range of policy choices.

Closed negotiations for large contracts are preferred by many (not all) international firms, some aid providing countries and politicians or officials who place great emphasis on tidiness and speed (or, alas, on under the table rakeoffs). In general - as illustrated in almost every African and Asian state the author has visited - the result is to raise costs. This is especially true when contractor finance or tied aid enter the picture or when there is evidence of corruption but it also happens when honesty is evident and speed or neatness is the developing economy negotiators' motivation. For a small economy in a hurry and with limited information to deal with a single large firm with greater (relatively and often absolutely) resources and financial opportunities, a much better supply of data and expertise, and less urgency as to time and place can rarely be to the developing economy's interest. This is not eliminated by requiring a company equity stake in the project - corporate and intercorporate incest on construction, management, purchasing, and sales can make the equity stake a minor cost of getting the contract not a compelling incentive to build the most suitable plant at the lowest cost or ensure reasonably satisfactory operation.

Open tender is not always a practicable course of action - shopping among alternative builders, manager, investors usually is. Comparing anticipated with actual costs for tender or quasi-open shopping on the one hand and closed negotiation cases on the other suggests the cost of a closed negotiation policy can often run at 50-150% of the attainable competitive price.

Oil refineries and pipelines, dams, water supply development, hospitals, highway construction, and (on a slightly different front) mineral and oil concession agreements are among the notable examples.

The need for freedom to bargain with alternative suppliers - vide the recent Economist article on initial and final costs and terms for the Zamtan Pipeline - enhances the case against heavy dependence on contractor finance. The sound contract can usually receive medium term bank credit if truly viable, the project able only to gain high cost short term money is probably a bad bargain in other grounds as well.

Turning to resources, all flows of scarce goods and services and of the purchasing power needed to effect their allocation in the desired pattern must be budgeted. This includes skilled manpower and government revenue as well as total domestic output, foreign exchange, and food supply. In the present context foreign exchange and foreign high level (and on occasion medium level technical) manpower are of the greatest direct interest.

### III

A plan like all budgets is drawn up for the future. It is a projection based on evaluation of what is likely to happen not a prediction or prophecy of what will happen. Moreover, projections of trends averaging good and bad years are usually more reliable than projections for individual years and one cannot really operate on average government revenue projections or average export earnings growth if the initial years fall below trend before any surplus to cushion such shortrun falls are amassed. (Herein, by the way, lies a very real cause of the inherent conservative strain in any responsible Central Bank's or Ministry of Finance's thinking. Caution can be overdone but to be over optimistic early in a year or a plan resulting in drastic subsequent cutbacks surely inhibits development more than initial caution allowing an assured programme to go forward with interim increases as and if resources are secured above initial anticipations).

Nowhere is uncertainty greater than on the external resources front. Export earnings, import costs (which are as critical as monetary export earnings in determining the real purchasing power of exports), foreign assistance, private capital flows - all are extremely volatile from year to year even when they appear to follow a satisfactory medium run trend. All too often the trend is also unsatisfactory leading to increasing external account stringency.

Let us take a few examples from 1961-1966 Tanzanian experience. Over that period exports (including those of Zanzibar) rose from £56 to £88 million - a 9% growth trend.

However, in three of the six years the actual export earnings diverged from the trend value for the year by 10% or more and the annual export increases varied from over 20% to minus 9%.

Imports grew from £55 million to £84 million. This would appear to indicate a 7% trend but in fact for the first three years the average increase was around 2 $\frac{1}{2}$ % and for the last three about 12 $\frac{1}{2}$ %. The range was from under 2% to almost 20%.

Aid data for (mainland) Tanzania from 1961/62 through 1966/67 estimate show sharp declines with only 1966/67 reading the 1961/62 level of £7 million and 1963/4 down to £2.6 million. Further, the proportion of grants has fallen from 45% in 1961/2 and 94% in 1962/3 to little over 20% in 1965/6 and under 20% in 1966/7. Absolutely grants attained a level of nearly £5 million in 1962/3 and have not reached £2 million in any subsequent year.

Commodity terms of trade data for extra - East African exports of (mainland) Tanzania have fluctuated sharply since 1961. However, taking 1961 (a depressed year) as a base they stood at 84 in 1965 and rose only to 90 in 1966. Income terms of trade - export proceeds divided by import prices - for Tanzania (mainland and Zanzibar) show the import of these price charges. From 1961 (base of 100) import purchasing power from export proceeds rose to about 145 in 1963 and 145 to 150 in 1964, fell to approximately 110 in 1965, and has only regained the 145 level in 1966 despite that year's 20% rise in export value over 1965 and 10% over 1964.

Because exports are a critical sector of domestic production and imports a key source of government revenue the erratic performance of the international sector has sharply aggravated the instability of domestic product and government revenue growth. Gross monetary domestic product from 1962 through 1966 may well have grown 7% a year on average after adjusting for domestic price changes. However, the range of annual growth rates is from minus 1% or more (1965) to at least plus 10% (1966).

The combined effect of tax revenue growth variations and foreign aid fluctuations on public investment (and therefore development plan implementation) is self-evident. Simply looking at public investment totals may hide the fact because the goal was for a rapid rate of increase and even the very bad result of 1965/6 did show a slight achieved increase over 1964/5. Once 1966/67 data are in hand the disparity of the growth in public investment in 1964/5 and 1966/7 as opposed to 1965/6 will be more evident and the impact of the 1965 export price - foreign finance drop on plan progress as well as domestic production and public revenue even more striking.



Uncertainty in the international economic sector - for trade, aid, and investment alike - is a fact of developing economy life. No plan which fails to face this fact and to provide means for living with it and limiting its impact on national development can be of much use or of much more than quasi-academic analytical significance.

The existence of comprehensive external uncertainty has been advanced as an argument against comprehensive economic development planning in African, Asian, and Latin American Economies. Given a high ratio of international trade to gross domestic product and of foreign financing to gross domestic investment, so this line of argument runs, "open ended" planning centering on a few key sectors but steering clear of overall targets and intersectional comprehensive is appropriate.

Superficially this criticism of comprehensive planning sounds reasonable. The greater the degree of uncertainty the more flexibility needs to be built into a plan if it is to be implementable over a range of actual foreign earnings and financing results. However, to argue in this way overlooks three facts. First a comprehensive plan overall projections is the only framework allowing even approximate evaluation of probable foreign balance trends and the sensitivity of the economy to fluctuations around the projected values. Second, in the absence of an overall analytical framework with data in relationships among projects and among the different sectors of the economy neither rational project alterations, additions, nor deletions to fit changing public sector financial situations nor soundly devised and consistent economic policies to affect private resource allocation and production decisions are likely to prove attainable. Third, "open ended" partial planning tends to result in developing planning becoming an echo of the very international economy weaknesses and uncertainties it is designed to overcome.

It is true that the addition or subtraction of projects from a limited number of sectoral plans - or a fortiori a colonial style shopping list "plan" - appears easier and neater than working through the impact of modifying one segment of a comprehensive plan involving an interlocking set of policies and projects. But the "ease" conceals the fact that the parallel policy changes, information on (and therefore the "need" to implement) which simply are not available from the limited sector, "open ended" approach to planning for economic development.

The importance and erratic behaviour of the foreign trade sector of the economy combine to make the best attainable projections a matter of priority for economic policy formulation. A comprehensive plan with detailed production (e.g. of export and import substitutes) and demand (e.g. imported consumer manufactures, capital

goods, foreign transport and travel) projections can provide at least an approximation of probable export and import trends and need for international aid and investment flows. It is no accident that the appearance of the first three comprehensive East African Development Plans over the period 1964-1966 parallels the rise of informed concern and specific policies relating to the medium run trade, capital, and external finance aspects of Kenyan, Ugandan, and Tanzanian economic development.

While the achieved 1969 to 1971 Tanzanian, Kenyan, and Ugandan balances of payments and international transactions are likely to diverge significantly from plan projections the projections provide far better indicators of what to expect than would ad hoc guesswork of simple extrapolation of past trends. Furthermore the same process that yields the projections helps provide data on how likely shortfalls or overfulfilment are in given external revenues or purchases and how sensitive the economic structure is to them.

In addition to reducing the degree of uncertainty surrounding future foreign economic transaction levels, a comprehensive plan provides a body of data and a framework for re-allocation altered (reduced or increased) flows of available resources through new policy and project patterns to achieve as much as possible of initial plan goals (as much more as possible if the real resource flow has exceeded expectations). The existence of the data and framework make a coherent annual operating plan (as opposed to an annual shopping list or cash account) possible and allow greater flexibility in phasing projects forward or back as resources and/or demand for them alters. Not only overall plan alterations but the relative size of different sub-period's programmes become more easily and efficiently alterable.

It is worth pointing out, at least in passing, that any coherent and efficient plan built up solely on the basis of individual projects and policies but modifying individual decisions to take account of their broader effects does in fact contain an implicit comprehensive development plan and strategy. This is, however, a very hard route to securing consistent and efficient resource allocation. Because it is an approach singularly unlikely to yield balance of payments projections the project by project method may also decrease the probability of arriving at a possible plan pattern. The foregoing is no argument against Project or policy evaluation. Rather it is an affirmation that they are most effective within a comprehensive plan laying down a coherent development strategy, a considered set of goals, and a consistent resource utilization framework.

#### IV

To argue that, in addition to providing a greater degree of predictability (a lesser degree of uncertainty), comprehensive planning

makes possible more rational adjustments to situations diverging significantly from projections has a series of policy implications. The first set relate to how resource shortfalls or windfalls should be allocated. Normally, all major sectors of the economy should share in the changes. The public development budget, the recurrent government expenditure level, private consumption, private investment, and the foreign balance account all will need to be altered directly or through policies influencing private discussion.

The development budget poses special problems. There is a temptation if growth in gross domestic production lags to try to push up the development budget. As at least one West African state which carried this approach quite far discovered, the result of trying to increase the absolute volume of public investment out of total resources less than those projected is almost certain to lead to popular unrest tied to falling consumer goods availability, radical deterioration of the external payments position, internal inflation, and a fall in private investment (domestic as well as foreign). In the case in point the results included a coup and a draconic decrease in development spending below the levels which could have been sustained had lagging growth not been "met" with public investment expansion.

On the other hand, to place the main burden of adjusting to a resource shortfall on development is also counter-productive. To do so ensures a continuation of the initial slump - vide a number of the smaller and poorer West African and South Asian economies whose public investment levels have been cut in relation to gross domestic product and whose economic growth rates have fallen to the 2% to minus 2% per year range.

Recurrent government budgets cannot normally - socially and politically - be cut back drastically under African conditions. The most satisfactory approach probably lies in seeking to hold recurrent expenditure growth to a ceiling not higher than a cautious projection of average annual growth of monetary domestic product. What is to be avoided is rapid increases in good years because funds are to hand and less rapid but positive increases in slump year as well on the grounds of stabilizing against declines elsewhere in the economy. Runaway increases in recurrent public spending in poor countries are consistent neither with high rates of investment, significant growth of per capita production, nor sustained increases in per capita personal consumption.

Private consumption must bear some of the impact of lower than anticipated resource availability. This is especially true when - as in Tanzania - it accounts for over two thirds of total resource use.

Otherwise the overall percentage shortfall in resources will have to be met by much higher proportionate cuts in investment and government recurrent expenditure if internal inflation and external payments crises are to be avoided.

What can be done is not to sustain overall private consumption but to seek ways of allotting it more bearably among different groups of consumers and to avoid unnecessary cutbacks in domestically produced consumer goods. There is normally no way to avoid substantial curtailment both of total consumption and of its imported component (with tax or quantitative measures to secure curtailment of consumer goods imports). There are ways of adjusting internal taxes and prices to broaden the sharing of burdens. For example if export price falls and drought reduce farmer incomes then it is highly unsound to increase either taxes paid by farmers or urban wages which will tend to lower prices paid to the farmer (as opposed to the distributor) still further and/or raise the prices of the urban goods he buys.

Private investment is particularly hard to influence in the face of unexpected resource short-falls. If these are expected to be brief it may well rise - as in Tanzania during 1965 - and help hasten recovery. Otherwise, the difficulties of devising policies adequate to the task of limiting private (especially foreign private) investment cutbacks are very grave indeed.

Foreign balance alterations are resultant on changes in resources availability not fully countered by changes in use. If an economy has adequate initial foreign reserves it can, and should, meet a portion of temporary shortfalls in foreign earnings growth by drawing on them or by short term borrowing. However, this requires careful distinction between short run swings around a trend and an altered trend and recognition that the converse of running down normal reserves (few developing economies have surplus foreign balances today, certainly no East African state does although equally none faces a reserve crisis) in slump years in building them up in "normal" or boom years.

Economics has been termed "the dismal science" and the foregoing may seem to justify that charge. Almost all of the examples dealt with shortfalls and cutbacks. Realistically this is the situation confronting policy makers and planners in most African economies. Deteriorating international trade and finance conditions and the perfectly correct - goal of seeking to plan for the maximum attainable development combine to produce this result. In any event, the same principle applies to windfalls as to shortfalls - the resources (additions in this case) they represent should be so distributed among

alternative uses as to make the largest possible contribution to present welfare consistent with raising the pace of development significantly.

V

The need to revise comprehensive plans comprehensively poses implications for economic planning, advising and decision making machinery. If individual decisions are prepared and taken in isolation not only is the comprehensive frame not utilized but the sum total of ad hoc alterations soon causes a loss of any initial economic policy coherence and consistency. Once again this has proven glaringly evident in several recent independent West African experiences in countries with quite different economic goals and political outlooks.

However, coherent and efficient policy-making and implementation does not mean unlimited centralization. Decentralization in plan revision as in plan formulation, in policy implementation as in project proposal, is vital. Working parties involving all interested experts - planning, implementing government body, parastatal, co-operatives, private business, labour, academic - are a useful device for increasing available information and judgement and for diffusing understanding as demonstrated by Uganda's experience in formulating Work for Progress. They should also be valuable in providing data and advice on policy and programme progress and effects and the need for revision.

Regional and local development committees - including planning, implementing ministry, local government, party and public, co-operative and private enterprise (including farmer) members - are critical. Central bodies are not ideally situated to know of local possibilities, to formulate flexible policy patterns, to publicise the plan in terms meaningful to enlisting mass support, or to respond to grassroots problems and possibilities rapidly. Local bodies - when integrated into an overall development effort - can make good these weaknesses.

Planning and policy are not the unique concern of one ministry (or two counting the Treasury with Devplan). If national development comprises all nationally agreed goals and development planning is the resource allocation pattern for attaining development objectives then a ministry with no effective planning unit is either saying its work is irrelevant to national development or that it is technically incapable of participating effectively in national development. Either has far reaching implications. Certainly neither Devplan nor the Treasury can nor should do the detailed technical and technico-economic work in all areas.

For example, Incentre and Impower quite rightly deal with industrial technical, market, and economic feasibility studies and work out incentive and protection policies within the overall industrialization and fiscal strategies.

Decentralised involvement in planning and policy decision taking requires centralized coordination and frame setting feasibility and consistence are to be maintained. At this level a case exists for a single responsible ministry combining the economic policy functions usually divided between a Treasury and a Planning Ministry. A logical threefold division of function exists within such an Economic Policy and Programme Ministry. Central are planning and policy formulation. Closely linked are resource (revenue) raising and expenditure implementation. Foreign aid and investment - for example - would fall in resource raising and detailed project feasibility studies and progress reviews in expenditure implementation. If combined with an effectively decentralized development administration such a ministry should not result in undue concentration of political or civil service power and should be of significant value in improving the quality and coherence of economic policy and its effectuation. The central manpower policy - for the entire economy, not simply the civil service - is logically an integral part of this functional cluster with recruitment a resource raising and allocation an expenditure area of crucial importance.

## VI

How can foreign financing be rendered more compatible with comprehensive national development planning and less contributory to uncertainty? The issues involved are complex both on the foreign resource transferring and receiving ends. That the present procedures are far from ideal is becoming almost an article of faith - if not **always** for the same or even compatible reasons.

Very great frankness and openness to new methods and ideas is required if the general belief that something must be done is not to deteriorate into making do from year to year in the hope that something will turn up (more crises and defaults most likely if that primrose path is followed!). The basic reasons for which resource transfers have been sought and provided have not been sound. What for example has £800 million of Western and Eastern arms credit done for Indonesia? For the USSR? For Western suppliers? What have Western European export guarantee loans achieved by furthering often unsound or ill considered, sometimes shady, and always high cost credit to, e.g. Ghana to the tune of £150 million? Surely neither the long term welfare of their own export sectors, the easing of their liquidity problems, nor the political or economic advance of Ghana.

Errors are not limited to the borrowers - resource providing countries have been quite as reckless, ill considered, and self defeating at the strategy, policy, project selection, and feasibility evaluation levels. Nor are they limited to politicians on either side - civil servants and economists have a very flawed record of advice. When they were right they have not pressed hard or cogently enough for more appropriate policies, when they were wrong they have all too often convinced political decision makers too well. (In the first context so conservative and quiet spoken source as the Economist has spoken "the treason of the trimming clerks.") Equally Development - Treasury battles have often been conducted as if maximization of power and of clashes not of national development and of mutually workable procedures was the end. True, planners are temperamentally and organizationally optimistic and may fail to see that to attempt too much is often to achieve less than is possible because over-optimism leads to resource mis-allocations including policies and projects suddenly cut off half achieved. But the orthodox Treasury - Central Bank caution can also result in an excess of caution not realizing that this too will often divert resources from more to less efficient uses and result in the failure to use some potentially available resources (including aid offers) at all.

A further general point is that the first step in improving aid and resource transfers value both quantitatively and qualitatively is to halt their 1961-1966 deterioration. Net aid and investment flows from all sources (gross transfers less repayment, interest, and dividends) to the Tiers Monde has declined slowly but steadily since 1961, especially if the handfall of petroleum rich economies are excluded. Given the supposedly agreed aim of 5% annual national product growth for developing economies ("the Development Decade") and the oft stated aim of industrial economies to use resource transfers to contribute effectively to that goal, the declining net transfer record is an absurdity. A 5% annual increase over the next two and a half decades would both fit the "1% of national product for aid" goal of O.C.D and UNCTAD and be consistent with bolstering rapid increases in developing economy internal savings and participation in world trade.

Terms in regard to interest rates and repayment have also deteriorated since 1961. Certainty in terms of period of commitment and of freedom from sudden cancellations has at best remained static. While flexibility in terms of plan support (versus project tied aid) and consortia approaches has made some progress this is by no means general and inflexibility in terms of ties to specific experts of the transferror for specific projects has grown apace.

Improvement of this qualitative record requires attention to at least seven points: training, "local cost" coverage, useability, terms, conditions, diversification, and liquidity creation.

Timing needs involve both certainty over time and flexibility within the period of an agreement. A \$5 million five year use period loan negotiated at the start of a planning period is much more consistent with serious and effective budgeting than five one year agreements eventually adding to the same sum. The loan's value is still greater if some degree of flexibility in annual drawings is allowed to offset windfalls and shortfalls in other sectors of development finance or physical implementation.

It is not self evident that such an approach would pose insuperable problems for lenders. Fewer negotiations would be a blessing all round. To secure budget approval for a limited number of larger, multi year commitments as opposed to a larger number of annual ones adding to the same sum should **not** prove bureaucratically or politically impossible - indeed it would avoid debates on each programme each year and allow a more serious examination of each of the more limited number of commitments on each year's agenda.

"Local Cost" is what a lender does not wish to cover and what a developing economy wants paid for from abroad if possible. That slightly nonsensical definition really is de facto what emerges from specific cases and even much of the general discussion of the issue. "Local costs" as usually defined are misnamed. Total cost less direct physical import cost of a project does not yield local costs in any meaningful sense. At least two varieties of "indirect import costs" remain.

First there are direct project related import costs both physical and human, capital goods and non-capital inputs into development projects. For example "local transport" largely represents imports of vehicles, parts, and fuels - only excise taxes and labour are truly domestic. Equally in many developing economies all domestic high level manpower is fully employed - any expansion requires direct project, indirect project, and project related importation of expatriate manpower whose salaries are dominantly remitted or spent on imports. Similarly their housing and transport have high import components (as do their offices and air conditioners). Even apparently local purchases, e.g. locally refined petroleum products often have a larger import than domestic content - in this case crude oil.

Second, once true domestic cost - largely unskilled labour, local raw materials, and value added in construction import processing - is isolated the multiplier import content of the project remains to be calculated.



The marginal import elasticity in most developing economies is high and attempts to reduce it to zero are hardly conducive to participation in expansion of world trade nor to maintaining reasonable internal price (or for that matter socio-political) stability. Thus in practice part of the domestic income generated by the project will end as an increase in consumer imports or of capital goods to expand local production of other consumer goods.

The change in focus such a separation of "local costs" into "indirect import costs" and "true domestic costs" can cause is major. In the case of Tanzania direct import costs of projects average perhaps 50%. Indirect project tied imports average at least 20-25%. Assuming a multiplier effect of two on domestic income generation the indirect increase in import demand from this source is likely to be at least 12-18% of initial project cost. In short the true import component is 85-90% not 50%.

The point is not that aid should cover 85-90% of all project costs. Quite apart from being normally unattainable any percentage significantly above the 50-60% range both hands over control of national economic policy to the "donors" and casts doubts on the seriousness with which efforts to mobilize national resources (including export earnings) are being pursued. Some portion of development expenditure can and should be covered by foreign exchange made available through export expansion or import substitution. What is to the point is that evaluation of the foreign exchange component of projects and plans should be realistic and complete. The whole foreign exchange component (not just the "direct physical import content") should be viewed as potentially aid worthy and the indirect project tied import costs should be viewed as normally to be covered in project aid provision.

From the developing economy point of view selling "indirect import content" should be easier than "local costs". Not only is the description true, it points out to the aid provider that there are additional resultant possibilities of exports from its aid. Further it poses the problem in terms of foreign account balance not internal governmental deficits, a method of presentation industrial economies are likely to view with greater sympathy.

Useability relates to what expenditures are seen as "aid-worthy". Surely aid should be to finance "development" (at any rate "economic development") not only "fixed investment". It is now accepted as a truism that fixed investment alone will not bring development in the absence of other "non-investment" expenditures. Yet aid policy still promotes a malallocation of resources to construction and machinery because non-capital development

expenditure while often viewed as "grant worthy" is grudgingly, if at all, regarded as "aid worthy" for loans or general support.

Feasibility studies, surveys, statistical services, recurrent costs of technical education, agricultural extension services, disease control and pest clearance to open up new areas or increase crop yields - all are investments in development which tend to be stinted of resources in comparison with more "normal" bricks and mortar type spending. This misallocation is at the very least, not alleviated by the fact that few of these types of spending are widely regarded as aid worthy.

Some progress has been made e.g. UNDP, AID on survey - feasibility study front, but not enough. Permanent centres and teams not once for all major project studies are needed and are by all economic logic at least as aid worthy as the physical projects their work shows to be viable. Most of these programmes require material and manpower imports to a very high proportion of their total cost. This suggests that there is little reason for balance of payments constraints - as opposed to a rigid and unrealistic capital equals development, recurrent equals consumption definition - to deter aid providing countries from supporting them as increasingly recommended by experts from a wide range of countries and organizations.

The main goal for terms can be stated very simply - a high proportion of 0-1% interest loans with 10 year grace and 25 to 40 years repayment linked to independent valuation (by whatever method) to ensure that the goods transferred are of a value equal to the loan. The latter proviso is critical - a low interest loan combined with a 50% markup on the true value of items provided is no great bargain as a number of countries have learned to their cost. The principle of securing either alternate offers or independent appraisals to guide price negotiations is no less critical in relations with overseas public bodies than with private firms. Furthermore, it is a workable principle - one can shop for projects and loan term packages (e.g. Czechoslovakia, East Germany, West Germany, and Italy all sell overlapping ranges of machinery and construction goods and services) and one can bargain with both Western parastatal (e.g. ENI) and Socialist State public sector corporations.

For the main body of development loans high interest and early repayment more less than no sense to lenders as well as borrowers. At least that is the case if the lenders seriously wish to promote the sustained development of the borrowers. It is quite incredible that the main body of developing economies will be able to dispense with net resource transfers before 2000.

This granted, repayments before that time merely hamper their long term resource and foreign exchange allocation planning and force the lenders to relend the same money. (that process raises apparent totals of aid voted and presumably maximizes parliamentary political problems). Interest charges have a similar effect - they merely raise the total the developing economies must ultimately borrow and reduce the net flow of resources resulting from any level of aid provision. The combination of a high proportion of short term loans with a relatively high level of interest charges has been a major factor lending to the Alice in Wonderland aid situation in which it takes all the running one can do that even to stay in the same place but to hold backward motion to a low speed.

The encouragement of developing economy use of a large volume of high cost short term contractor finance by industrial economy export promotion schemes or state trading corporation credits has been and remains utterly irresponsible and misguided. One can only hope that the recent rash of defaults or quasi-defaults and refinancings cum moratoria on the one side, and dislocated economies following draconically depressionary policies on the other, will be seen as telling evidence in this regard by lenders and borrowers alike.

None of this is to argue that diversification of aid terms, sources, and types is unsound. Quite the reverse if there is careful evaluation of what resources transfer terms fit any specific case. Private or quasi-public medium term credit is appropriate to some ventures. The Tanzam pipeline involving the ENI group and Mediobanca and providing 15 year, 6-6 $\frac{1}{2}$ % credit is a case in point. Such a project can carry that interest rate and repayment schedule. Similarly a short to medium period commercial loan can be valued if the assets can really provide an appropriate profit and cash flow pattern vide the Zamtan Road company.

The same sort of imaginative case by case examination can go into loans directed to parastatal corporation needs. For example NDC might borrow to finance industrial projects partly drawn in machinery and personnel imports and partly in goods whose sale during the construction period could both cover domestic construction costs and at the same time be used to build up the selling organization and experience of the firm until its own production came onto the market. This approach could, among other gains, reduce the disadvantages of an "export tied" loan to a minimum for the borrower and minimize adverse foreign balance results for the lender.

Diversification should also involve broadening any developing economy's significant sources of resource transfers - private as well as public - and reducing the dependence on any single source.

Dependence on a single source of funds cannot but add to uncertainty because of the possible shifts in that industrial economy's economic and balance of payments situation quite as much as its political policies or interests. Freedom to bargain for aid terms and project prices can be significantly expanded and trade patterns made less arbitrary and more economic if resource sources are broadened.

For aid providing states the reverse policy of providing significant assistance to many states and dominating the aid flows to none would also offer advantages. For one thing it would spread and probably stabilize their trade with developing economies. For another it would leave them less vulnerable to sudden requests for massive aid increases if a handful of developing economies meet major setbacks and less open to demands of the "if you don't help us we will surely sink" variety. Dependence has adverse implications for the dominating power - once committed it is less able to argue for economic rationality and probably less able to exert influence for change except at such a draconic level of pressure as to arouse intense resentment rather than serious policy re-evaluation. Neither the record of those states whose aid comes almost entirely from one of the two largest aid donors nor that of those looking primarily to the other suggests that such concentration has a beneficial result on the

developing economy's policy choices or the long term international economic (or even political in at least one of the two groups) interests of the aid provider.

Conditions on aid are a vexed subject. Only two will be considered here - tying and plan or project support. Tying of aid to projects in the negotiating phase and tying of aid to exports of one country at any point are undesirable from the developing economy point of view. They lower flexibility and raise costs. From the aid providing country's point of view balance of payments constraints may require at least some export tying and - less reputably but in at least three major lender cases significantly - non-competitive or declining industry defense call for project tying.

The greatest harm arises when project ties are linked with export ties. Then no freedom to purchase the project's import component (whether direct or indirect) in the best market not to use the tied aid to purchase the most competitive goods available in the aid providing country exists. This form of multiple tie can and should be ended. Surely aid programmes are not the appropriate method of bolstering the weaker sectors of an economy at the cost of the "aided" countries. If the industries are to be supported it would be far better to give them subsidies allowing them to compete for aid contracts and showing the cost as an internal subsidy not external aid.

Plan support aid through consortia "aid groups" offers possibilities for reducing aid limitations and conditions to all participants' advantage. In such a forum careful examination of overall goals and needs can be conducted in a pragmatic, economic context limiting political clashes and simple misunderstandings or miscalculations.

Once a number of overall commitments from a number of countries has been obtained it is much easier to agree on purchase patterns consistent with efficient buying and avoiding significant foreign balance problems for any one lender. Equally both long term commitments and flexibility in annual drawings should be easier to achieve in such a framework.

Certainly consortia are not a cure all for the problems of foreign aid on the one side and foreign resource procurement on the other. They do offer a means by which progress can be made if the precondition of a reversal in the decline of net aid is met.

Liquidity and international reserves are often mentioned in the context of aid but not usually with the appropriate emphasis. There is a set of economic myths that developing economies all follow inflationary and payments' deficit maximizing policies, may need additional reserves but only to spend on development, and can best be forced to follow "sound" policies when short of reserves. With all respect this is nonsense and arrogant nonsense at that.

Many developing economies follow rational or even cautious policies both on the domestic and international balance fronts. Indeed, a number of industrial economies have rather more dismal and less responsible records. International reserves are needed primarily as a safeguard against short run international transaction **fluctuations** and therefore the quantity of reserves needed rises as transactions grow. If developing economies are to participate in broadening and expanding of world trade they will require increased reserves to hold. A shortage of reserves does not promote responsible policies. In practice it usually leads to autarchy, sky high tariffs and quantitative restrictions with resultant profiteering - corruption - administrative breakdowns, internal inflation, growing foreign balance stringency, and often an internal socio-economic crisis leading to recurrent revolution. An alternative pattern is rigid internal austerity, stringent controls on most forms of external expenditure, and an acceptance of a growth rate for production less than that of population or even less than zero - in developing economies another road to recurrent crisis and governmental changes. Neither of these precisely meets any definition of sound economic policy.

The basic global liquidity problem is well known. International trade is rising on a 6-8% yearly trend. Global reserves should therefore rise at least 4-6% a year. New gold can raise them at most 1% a year. Willingness to hold more of the two reserve currencies - US dollars and UK pounds - is near nil. Thus unless a new reserve unit or new unconditional drawing rights with the IMF (or an increase in the price of gold - a bad and an unlikely choice) is agreed upon, reserves will fall as a proportion of world trade and a liquidity crisis ensue within five years.

The results of such a crisis for developing economies would be severe. Concern over balance of payments by industrial economies would lead to aid cuts, tighter tying of aid to exports, internal deflationary policies leading to industrial setbacks which would worsen demand for primary products and cut developing economy export earnings. The UK and US reactions to their balance of payments problems indicate all too clearly what a world liquidity crisis and a halt in industrial economy growth would mean for Tiers Monde development. 0-2% rates of domestic product growth could well become the norm with negative ones far from uncommon.

Quite apart from their interest in averting a global liquidity crisis developing economies in general - there are a few exceptions such as Zambia, Malaysia, Libya, Kuwait - need to expand their foreign reserve holdings to keep them at a safe level in relation to growing international transactions. After all, the larger the volume of transactions the larger absolutely are likely to be the short term deviations reserves are needed to cushion.

For example Tanzania's reserves now stand at about 33 $\frac{1}{3}$ % of average 1964-1966 annual imports. However, if the 1971 ratio of reserves to 1968-1970 average imports is to be maintained reserves must rise by up to £10 million. To do so within the present world reserve system would either require borrowing £10 million abroad specifically to bolster reserves - a form of aid which is almost literally unheard of whatever its possible merits - or reduce imports by £10 million with resultant cutbacks in living standards and development. In short in the absence of either internal inflation or balance of payments deficits a restrictionist policy would be needed resulting in lower growth and wasted red resources. That would not be financial prudence but fiscal and economic madness resulting directly from the present world monetary system.

In practice Tanzania is better off than many developing economies. 33 $\frac{1}{3}$ % is a rather high ratio of reserves to imports judging on the basis of probable fluctuations.

Up to £2-3 million may be added (once for all) to the reserves by methods other than those cited. However, that may merely postpone the problem to 1975, it certainly does not solve it.

Solution can only lie in a regular examination - say at five yearly intervals - of global trade growth trends and resultant reserve needs. The amount of the reserve increase not available from new gold could then be created in the form either of unconditional IMF drawing rights (borrowing power to meet short term crisis unseable at the discretion of the IMF member) or, preferably, of new international reserve units. Either should be paid for by deposit of national currencies with the IMF and either should be allocated to IMF members in relation to their existing IMF quotas which are in rough relation to economic size.

Proposals that developing economies should not receive such rights or units - or receive them indirectly or on special (less favourable) terms - are wrong in principle and practice. They amount to asking the poorer nations to subsidize liquidity creation for the rich and are usually defended by the triple myths cited earlier. Developing countries need reserves to hold, they are full participants in international trade, they would bear any costs resulting from reserve misuse by industrial (or developing) economies. They have every right to demand that liquidity creation take account of these facts.

Liquidity may seem an aside in a discussion of planning and foreign finance. It is not. Everything that can be achieved by more flexible and better organized comprehensive planning better related to a revised and improved system of international finance transfers could be wiped out by a world liquidity crisis. Everything and more.

The emphasis on improved aid quality stems from the fact that there is no reason to expect sharp increases in quantity over the foreseeable future. Greater developing economy reliance on national resources is essential. Its corollary should be to improve the quality of external resource transfers so that they form a more effective complement to national efforts.

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