The Emergence of UNCTAD[1]

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Conceptual Origins

From the very beginning the governments that established UNCTAD undertook a commitment 'to lay the foundations of a better world economic order' [UNCTAD 1964:para 9]. They recognised that 'international trade is an important instrument for economic development' [UNCTAD 1964:para 53]. In view of the importance attached to these basic ideas by those who were most active in creating the new institution, it is natural to begin by examining their origins and the character of the new departure that they represented.

The conventional wisdom about international trade, then as now, was grounded in neoclassical political economy, which asserted that spontaneous market forces were always tending towards a benevolent equilibrium, and that any departures from this equilibrium would inevitably set in motion a self-correcting process of adjustment. Moreover, full employment, economic growth and the optimum utilisation of resources were assured.

The first major challenge to neoclassical political economy was that of the Keynesian school in the 1930s, which showed that cyclical fluctuations in the level of output and employment were inherent in the system. Since spontaneous forces could not be relied on to eliminate the ups and downs of the trade cycle, it was incumbent on governments to provide the economic management needed to maintain full employment at all times. At the San Francisco and Bretton Woods conferences governments expressed their determination to avoid a return to the conditions that had brought about the Great Depression of the 1930s. Accordingly, the charters of the United Nations and of the International Monetary Fund embodied a commitment to the full employment objective.

There was no corresponding enlightenment or freshness of outlook with respect to world trade. In this area the old neoclassical precepts continued to prevail. Whatever happened in world trade had to happen by virtue of an international division of labour that was as inescapable as it was just.

The prevailing view in the first post-war decade was that if governments would only renounce the manipulation of exchange rates and dismantle the restrictions on trade and payments left over from the depression and the war, market incentives would be set free and would operate in such a way as to ensure the specialisation of all countries along the lines best calculated to promote their development, based on the principle of comparative advantage. Indeed, the spontaneous forces in the system could be relied upon, in the long run, to bring about not only universal development but the progressive equalisation of incomes worldwide, so that inequities in the intercountry distribution of income would disappear of their own accord. Thus while the attainment of full employment called for government intervention in the economy where needed, in international trade and payments the objective was in exactly the opposite direction.

To this vision of the world economy there emerged, soon after the end of World War II, a centre of strong opposition. This was located not in an academic institution, as the Keynesian school had been, but in the United Nations Economic Commission for Latin America (ECLA), headed by Raúl Prebisch, who was later to become the first Secretary-General of UNCTAD. Prebisch confronted the conventional wisdom head on. So far from there being any spontaneous tendency towards a worldwide levelling of incomes, he showed that the forces tending towards the continuous polarisation of economies, both internally and externally, were far stronger than those tending towards equilibrium. He demonstrated that if these cumulative forces of the world economy were not countered by deliberate action at the national and

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international level, the economic distance between rich and poor would grow even wider.

The power of initiative and change rested with the industrial countries at the centre of the world economy while the less developed countries at the periphery merely responded passively to the stimuli generated at the centre. The hegemony of the centre was, moreover, manifested both in the composition of its trade with the periphery and in the terms on which that trade took place.

The composition of trade was a survival of the old colonial order under which the metropolitan powers exported manufactures to their dependencies in exchange for imports of foodstuffs and raw materials. This pattern of specialisation was promoted and preserved by the tariff structure of the industrial centres: while primary products were generally admitted duty free or at a low rate of duty, tariffs on manufactured imports were deliberately set to increase progressively with their degree of manufacture. This relic of mercantilism had survived into modern times.

Structural rigidity in the composition of trade between the centre and the periphery had major implications for the growth and terms of trade. In the first place world demand for primary commodities tended to increase much more slowly than for manufactures. This was due partly to the fact that advances in real income were generally associated with relatively slower increases in the demand for foodstuffs and other staple consumer goods and a shift in demand towards industrial goods and services. Moreover, technical progress was constantly tending to reduce the raw material content of final output by making it possible to ecomomise on the use of raw materials as well as by increasing the degree of fabrication of finished products. The development of synthetic products in the industrial countries further reduced the requirements of these countries for imports of natural materials from developing countries. Finally, the industrialisation of agriculture in the developed countries made it possible for them to do without a number of the agricultural products previously imported from developing countries.

The Terms of Trade

Coupled with the above trends was a tendency for the terms of trade of developing countries to deteriorate over time owing to declines in the prices of the primary commodities exported by them in relation to the prices of the manufactures that they imported from the industrial countries. Of the entire body of thinking developed by Prebisch and the ECLA school, this particular proposition was probably the most controversial, and became the subject of an extensive literature.

This is not the place for an in-depth review of the debate on the unequal terms of exchange, as it has been called. In part, the critics misunderstood what Prebisch was saying. As he pointed out in his report to UNCTAD I,[2] the terms of trade thesis 'should not be regarded as an immutable law'. Indeed, Prebisch pointed to the circumstances in which the inherent tendency towards deterioration might be offset or even reversed.

Consequently, much of the controversy about the historical trends was beside the point. Since Prebisch was not arguing that relative declines in the prices of primary products would take place under any and all conditions, but only that there was a *tendency* for this to occur in the absence of countervailing forces, it was not necessary for him to show that historical trends had invariably been in that direction.

It is true that in the course of his original exposition of the thesis in 1950, he cited data that indicated a long-run improvement in United Kingdom terms of trade from 1876-80 to 1946-47. Since UK imports consisted predominantly of primary commodities while its exports were mainly manufactures, he drew the conclusion that developing country exporters of primary commodities had suffered a symmetrical deterioration in their terms of trade. This reasoning has been criticised in the literature on various technical grounds, some valid, some invalid. It should, however, be borne in mind that the statistical evidence available to Prebisch in 1950 was extremely limited, and any alternative series that he might have used at that time would have been at least equally open to criticism.

More important, however, is the fact that empirical results for *any* period, however well based in statistical terms, could yield only suggestive and not conclusive evidence. The perceived trend in the statistics for any particular period should, properly speaking, be the starting point for further analysis of *all* the various factors involved, including both the inherent factors emphasised by Prebisch and the countervailing factors — if any.

It is therefore the analytical case that must be decisive, and here there can be little doubt that the general proposition advanced by Prebisch has been vindicated. As recently demonstrated by Professor Spraos, [1983] rigorous analysis of the Prebisch thesis, reinterpreted as relating to the double factorial terms of trade, shows that 'the exchange of primary exports against

[2] The term UNCTAD I is used to denote the first United Nations Conference on Trade and Development.

manufactured imports has been conducive to making growth incrementally inequalising for developing market economies'. This conclusion emerges quite simply from the fact of the low income and price elasticity of demand for the primary commodities principally exported by the developing countries. It is reinforced by the fact that while technical progress in the manufacturing industries of developed countries usually generates higher real wages and profits for the producers, corresponding advances in the technology of primary production tend to be passed on to consumers in the form of (relatively) lower prices.

Adverse Trends in World Trade

At the level of international economic diplomacy, the most important factor in the convening of UNCTAD I was the progressively deteriorating situation of developing countries in world trade in the course of the 1950s and early 1960s. The contribution of the 'ECLA doctrine', as it came to be called, was that it was able to show that the adverse trends were not casual or accidental, but were deeply ingrained in the world trading system itself. While world trade as a whole more than doubled from 1950 to the early 1960s, exports of developing countries rose by only half. As a result, the share of developing countries in world trade declined steadily from nearly one-third in 1950 to only slightly more than one-fifth immediately before the Conference. The developing countries lost ground even in world trade in primary products in which they were believed to have a comparative advantage. Thus the share of developing countries in world exports of primary commodities other than petroleum declined from 41 per cent in 1950 to less than 30 per cent in the early 1960s.

Some of the inherent factors tending towards this outcome have already been mentioned — notably the lower income elasticity of world demand for primary products exported by developing countries than for manufactures, exported mainly by developed countries, and differences in market structure as between the two product groups. But there were additional factors tending in the same direction. Prominent among these were the restrictions on imports of primary commodities imposed by industrial countries, particularly in connection with agricultural support programmes. At the same time, the developing countries made little headway in manufactures: in fact their share in world exports of these goods was also declining. The main factor in this decline was the recovery in the export capacity for manufactures that had taken place in Western Europe and Japan, which was only to be expected. The developing countries were, however, concerned about various obstacles to their export trade in manufactures. In addition to maintaining the old colonial tariff structure, as noted earlier, the developed countries were beginning to take even more stringent measures against manufactured imports from developing countries, particularly cotton textiles.

In 1962 the developing countries found themselves compelled to enter into an international arrangement for the restriction of cotton textile exports to the industrial countries under the threat that in the absence of such an arrangement the latter countries would impose even more severe import controls. This new development was clearly an ominous one, giving rise to the fear among developing countries that any success they might achieve in diversifying their exports into the field of manufactures would quickly meet with strong and discriminatory resistance from the developed countries.

These various obstacles to the growth of exports of developing countries were compounded by a deterioration in their terms of trade: between 1950 and 1961, for example, the terms of trade of developing countries deteriorated by some 17 per cent. One did not have to accept the theory of unequal exchange to see that the persistence of this trend would cause mounting difficulties for the developing countries.

The Trade Gap

It was not surprising in these circumstances that the export earnings of the developing countries should have been increasing much less rapidly than their import requirements. The issue of the 'trade gap' of developing countries, and the consequential foreign exchange constraint on their development, was dramatised forcefully by the Conference and placed firmly in the centre of international economic discussion.

In launching the first United Nations Development Decade in 1961 with the strong support of President Kennedy and other leaders of industrial countries, the General Assembly of the United Nations had adopted the target of a minimum annual rate of growth of five per cent in the real income of less developed countries by 1970. This rate of growth was certainly not an inordinately ambitious one, and was not, in fact, much higher than the average rate of 4.4 per cent per annum recorded in the 1950s. In view of rapid rates of population increase, the target rate of growth of five per cent per annum corresponded to an annual rate of expansion of little more than two and a half per cent in the average *per capita* income of the developing countries. For the poorer countries that accounted for about half of the population of the less developed areas, such a rate of growth implied that the period required to reach contemporary Western European living standards would be of the order of two hundred years.

The report of the Secretary-General of the Conference to UNCTAD I drew attention to the foreign trade implications of this minimal five per cent growth target. On the basis of past experience, an overall growth rate of five per cent per annum would necessitate a rate of increase of import volume of not less than six per cent per annum. One of the main reasons for this was that any acceleration in the rate of growth would necessitate additional investment, and the import content of such investment was normally much higher than that of income as a whole because developing countries had relatively little capacity for production of machinery and equipment.

On the other hand, the volume of exports of developing countries had been increasing at a rate of only four per cent per annum during the 1950s, and if petroleum exporting countries were excluded the rate was even lower. At the same time, the effect of the deterioration in terms of trade was that the purchasing power of exports over imports rose more slowly still, by under two per cent per annum.

This, then, was the basis for the 'trade gap' of developing countries. Even at existing rates of growth there was a widening gap in the balance of payments of developing countries. At higher rates of growth consistent with the quite modest objectives of the Development Decade, the gap would be magnified accordingly. It was estimated that if current trends in world trade continued, the trade gap of developing countries would be likely to reach an order of magnitude of about $20 bn by 1970, a daunting figure at the dollar prices prevailing in the early 1960s.

Projections of this type have since become commonplace, and are now carried out regularly not only by research departments of the United Nations but also by those of other international agencies such as the IMF, the World Bank and the OECD. At the time of UNCTAD I, however, the idea of a quantifiable foreign exchange constraint on growth created fierce controversy. Strong intellectual artillery was mounted against the idea of a trade gap on the basis of a variety of arguments ranging from fundamental criticism of the concept itself to scepticism about the statistical techniques employed.

There was, of course, room for honest differences of opinion as to the precise magnitude of the 'trade gap'. Being a residual, the gap between projected exports and imports was necessarily sensitive to the underlying assumptions made about the functional relationships between trade and growth in both developed and developing countries. But it could hardly be doubted that there *was* a gap, and that it was tending to increase. This was obvious from the fact that the volume of exports of developing countries was tending to rise more slowly than the volume of imports. This factor alone indicated a growing trade gap even if there was no further deterioration in terms of trade.

Closing the Trade Gap

What was important was not the precise magnitude of the 'trade gap' that had been projected, but the basic tendency that it indicated. It pointed clearly to the character of the measures that would be needed if the General Assembly's target rate of growth were to be realised. Either the 'gap' would have to be bridged by a suitable expansion of trade or aid, or the developing countries would have to effect a fundamental reorientation of their foreign trade pattern and possibly of their domestic economic policies as well. The only other alternative was a reduction in overall growth rates by the developing countries to the point at which their imports would rise no faster than the current slow rate of expansion of their exports — and this would mean the collapse of any hope for attainment of the General Assembly's objectives.

Part of the opposition to the 'trade gap' analysis was based on concern in the developed countries that it was intended thereby to establish a case for $20 bn of additional aid annually. It is quite clear, however, that this was *not* Prebisch's intention. His main objective was to obtain acceptance of the proposition that the trade and aid objectives of the international community must be consistent with its growth objectives. Such consistency could, however, be achieved in various ways. Addressing the Federal German Society for Foreign Policy in Bonn in June 1965, for example, Prebisch said: 'Allow us to export that much more and we will be a ready market for an additional $20 bn worth of your industrial products per year'. A few days earlier he had told the Canadian Manufacturers' Association in Toronto that 'the fundamental long-term solution [to the problem of the trade gap] lies in trade — by increasing the possibilities of the developing countries to export more, so that they can import more'. Aid, he said, could only be a temporary measure, though it might have to continue for some time for countries at a very low level of development.

Convergent Measures

How could such a transformation of the trade prospects of developing countries be accomplished? The answer lay in a programme of what Prebisch called 'convergent measures' — mutually supporting measures by both developing and developed countries. Great efforts by the developing countries themselves were indispensable — 'the policy of international cooperation is only complementary, it cannot be a substitute for internal development policy' [Prebisch

1964:113]. In particular, effective steps would have to be taken to deal with the three main obstacles to the growth of productivity and *per capita* income in developing countries: land tenure; limited social mobility and the ignorance of the masses; and the concentration of income in the hands of relatively small population groups [Prebisch 1964].

Prebisch was also very much aware of the cul de sac that Latin American countries had got themselves into by pursuing policies of what he called 'inward-looking industrial growth, regardless of the outer world'. He considered that 'the countries now embarking upon industrialisation should be warned against the grave mistakes we have made in Latin America because we were unable, within the framework of world production and trade, to start exporting manufactured goods at the very outset of our industrialisation process' [Prebisch 1963].

But if developing countries were to be encouraged to adopt more outward-looking policies, the international community must be ready to accept the implications for world trade and make room for the additional exports involved. 'It is no good', said Prebisch, 'to preach the need for [developing countries] to develop by their own efforts and at the same time to limit their possibilities of giving practical expression to that effort in the international field through the expansion of their exports. They must not be forced into a kind of closed development' [Prebisch 1964:124].

Commodity Stabilisation

Since the unregulated operation of market forces had been tending to bring about perverse transfers of real income from the poor countries to the rich, there was a strong case for corrective international action to counterbalance this process. Such action could take the form of internationally agreed measures to stabilise trade in basic commodities at a reasonable level of prices, and to promote the diversification of exports of developing countries so as to include a progressively growing proportion of manufactured products.

The industrial countries were aware, from their own experience, of the serious problems of domestic income distribution resulting from the chronic weakness of agricultural prices, and the consequent persistent tendency for the internal terms of trade to move against the agricultural producers. It was for this reason that they had taken a variety of steps to support domestic agricultural prices or incomes through deliberate government regulation of commodity markets or provision of income supplements to farmers. They were nevertheless opposed to international intervention in commodity markets. While their opposition could be understood in terms of their short-term interests, it was less clear that it was rational in a longer run perspective, since rising real income in the developing countries was clearly in harmony with the interests of the developed countries from many points of view, including the larger markets for their exports that a prosperous Third World would imply. In fact, however, the policies of the industrial countries on agricultural production and trade had a doubly adverse effect on the developing countries. While their *laissez-faire* policies at the international level prevented the adoption of agreements to stabilise international commodity prices, their close regulation of internal agricultural markets created a stimulus to domestic producers and an additional obstacle to exporters in developing countries.

It was therefore not sufficient to expand the number and increase the effectiveness of international commodity agreements. It was also important to improve the access of primary commodities produced in developing countries to the markets of the industrial countries. Barriers to imports of such products should be progressively reduced and ultimately eliminated.

Export Diversification

But the real solution to the problem of insufficient growth of exports from developing countries lay in diversification of exports, particularly into the field of manufactures. Here there was a need for preferential treatment for the manufactured exports of developing countries in the markets of developed countries. The case for such preferences was that they could help in overcoming the initial difficulties and high costs of breaking into highly competitive markets in which established large-scale industries in the developed countries had an overwhelming advantage. In other words, the case for preferences was a logical extension of the generally accepted argument for the protection of infant industries through import tariffs. In fact if infant industries needed protection in the domestic markets of developing countries because of their initially high costs of production, they obviously needed even more protection in foreign markets, whether developed or developing, in the form of preferential treatment.

Industrial growth in the developing countries could also be accelerated through concerted action within regional groupings of these countries, thereby increasing the scope for efficient import substitution by bringing into play the benefits of specialisation, competition and economies of scale.

These were among the main features of a new world trade policy that would make a significant positive contribution to world development instead of creating obstacles to that development, as had too often been the case in the past.

The Role of Trade in Development

One of the major achievements of UNCTAD I was its acceptance, in principle, of the importance of trade as an engine of development. The very first paragraph of the Final Act of the Conference states that 'In an age when scientific progress has put unprecedented abundance within man's reach, it is essential that the flows of world trade should help to eliminate the wide economic disparities among nations'. That declaration reflected a new concept of international trade. As noted earlier, world trade had hitherto been viewed as the spontaneous and benevolent result of the operation of market forces. International action should therefore be limited to the creation of the freest possible environment for trade and payments, so that the beneficial effects of market forces could be maximised.

Now, however, it was gradually coming to be understood that international trade could and should be shaped to the goals of international policy. The Conference thereby marked a turning point in attitudes to the role and possibilities of international trade in promoting development in all countries, and especially in developing countries. The extent of the change should not, of course, be exaggerated. Whatever the texts agreed to at UNCTAD I may have contained, it certainly cannot be said that they embodied international agreement on the specific steps needed to promote development through trade. Indeed even today, a generation later, the battle for better access for the exports of developing countries to the markets of industrial countries remains to be won, and in some respects the protectionism of the latter countries is even stronger in the 1980s than it was in the 1960s.

Objectives of the Socialist Countries

The socialist countries of Eastern Europe had long had their own reasons for urging the convening of a world economic conference devoted particularly to international trade problems. At the United Nations General Assembly in 1956, the USSR delegation proposed that such a conference be convened in the following year to consider 'a further expansion of world trade and the establishment of a world trade organisation within the framework of the United Nations'.[3] A draft resolution calling upon the Economic and Social Council to consider the idea of a world economic conference was narrowly rejected by the Assembly's Economic and Financial Committee.[4] At frequent intervals thereafter the socialist countries continued to press their case, and when the developing countries began their own campaign for a conference on trade and development in the early 1960s, the two groups joined forces in furtherance of this objective.

The principal motivation of the socialist countries in this regard derived from the fact, as they saw it, that they were subject to trade discrimination by the OECD countries as well as by many developing countries. It was true that most of the developed market economies had granted most favoured nation tariff treatment to the socialist countries. But the latter were concerned about cases of continuing tariff discrimination, and particularly about the EEC and EFTA programmes of mutual tariff reduction under their respective customs union and free trade area arrangements, which the socialist countries regarded as tantamount to raising barriers to traditional east-west trade.

They were even more disturbed by the widely prevalent practice in OECD countries whereby imports from socialist countries were subject to quantitative restrictions, and certain exports were subject to 'strategic' export controls. The socialist countries were also confronted with varying degrees of restriction on transferability of the currencies earned from exports to certain of the developed market economies. In the light of these considerations, the primary goals of the socialist countries were the mutual application by all countries of most favoured nation treatment in relation to both tariff and non-tariff restrictions, and a more flexible payments system. These objectives could not, they felt, be attained by means of negotiations within the General Agreement on Tariffs and Trade (GATT) to which they had not (except for Czechoslovakia) subscribed. As they saw it, GATT rules had been drawn up one-sidedly, reflecting the needs of market economies. State trading was treated in GATT only from the limited standpoint of the special conditions obtaining in a few relatively unimportant sectors of the market economies themselves. There had been no attempt in GATT to establish a mutually satisfactory regime for east-west trade.

The OECD countries, on the other hand, were concerned about the difficulties of giving any real meaning to the concept of non-discrimination in the context of a centrally planned economy. For example, they considered it virtually impossible for any external authority to ascertain either the criteria determining governmental trading plans and policies in the socialist countries or the methods whereby such

[3] UN document A/P.V.589, para 125.

[4] UN document A/C.2/L.319, A/3545, para 15.

criteria were translated into choices between competing sources of supply made by the agencies responsible for import decisions. On the other hand they insisted on the legitimacy of the EEC and EFTA arrangements insofar as they observed the principles for such arrangements laid down in GATT.

The socialist countries made common cause with the developing countries in seeking a world trade conference, in the hope and expectation that the east-west trade issues in which they were interested would find a place on the agenda of the conference as well as in the work programme of any institution that it might establish. Prebisch's report to UNCTAD I did in fact contain a short section on east-west trade. While the report did not propose any specific solution to the controversy between the socialist countries and the developed market economies, it did support efforts to resolve that controversy. It pointed out, moreoever, that 'World trade is an intimately interrelated network, and the repercussions of obstacles in any one part are felt inevitably in all the others' [Prebisch 1964:92].

The developing countries had no objection to the discussion of east-west issues in UNCTAD and supported the socialist countries on the principle that east-west trade should be normalised. The OECD countries, however, did not regard UNCTAD as an appropriate forum for discussion of east-west issues and preferred to take these issues up in the UN Economic Commission for Europe. The developing countries, for their part, saw no reason to press the OECD countries on this matter. On the contrary, they feared that prolonged and acrimonious debates on this subject might divert attention from the questions of trade and development that they considered of highest priority. Moreover the exports of socialist countries to the OECD countries consisted largely of primary commodities and were therefore, to a considerable extent, in competition with the exports of developing countries. The developing countries were therefore concerned that any expansion of east-west trade should not be at the expense of developing country exports.[5]

Furthermore, developing countries expected the socialist countries to undertake specific trade and aid commitments within the framework of their planning processes. They should, for example, accelerate the growth of their imports from developing countries, reduce the differential between the import and domestic sales prices of commodities purchased from these countries, grant concessions equivalent to the preferential arrangements expected of the market economies, and refrain from re-exporting commodities imported from developing countries except with the permission of the latter. These and other requests addressed to the socialist countries placed them, in effect, in a position similar to that of the developed market economies *vis-à-vis* the Third World, and their role in UNCTAD gradually evolved accordingly.

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[5] This concern was later voiced explicitly in the Algiers Charter, TD/38, 3 November 1967.