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ECONOMIC DEVELOPMENTS IN
SOUTH AMERICA

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ECONOMIC RELATIONSHIPS
OF THE
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CONGRESS OF THE UNITED STATES



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LETTERS OF TRANSMITTAL

JULY 20, 1962.

To the Members of the Joint Economic Committee:

Transmitted herewith for the use of the Joint Economic Committee, and other Members of Congress, are the summary comments of the Subcommittee on Inter-American Economic Relationships, on their recent hearings on "Economic Developments in South America."

Sincerely yours,

WRIGHT PATMAN,
Chairman, Joint Economic Committee.

JULY 19, 1962.

HON. WRIGHT PATMAN,
*Chairman, Joint Economic Committee,
U.S. Congress, Washington, D.C.*

DEAR MR. CHAIRMAN: Transmitted herewith are summary comments on our hearings May 10 and 11 on "Economic Developments in South America" which we consider appropriate to make to the full committee. The printed record of testimony has previously been made available to members of the committee and to the public.

We wish to thank the witnesses for their excellent papers and observations. The participating witnesses were:

Prof. William S. Barnes, Harvard Law School.

Mr. Seymour Brandewein, AFL-CIO.

Mr. William F. Butler, Chase Manhattan Bank.

Prof. Tom E. Davis, University of Chicago.

Mr. John F. Gallagher, Sears, Roebuck & Co.

Mr. Leonard Kamsky, W. R. Grace & Co.

Mr. and Mrs. Milic Kybal, Washington, D.C.

Mr. Peter R. Nehemkis, Whirlpool Corp.

Prof. Raymond J. Penn, University of Wisconsin.

Mr. Rodman C. Rockefeller, International Basic Economy Corp.

Sincerely yours,

JOHN SPARKMAN,
*Chairman, Subcommittee on
Inter-American Economic Relationships.*

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ECONOMIC DEVELOPMENTS IN SOUTH AMERICA

INTRODUCTION

The tremendous significance which the economies of the Latin American countries have to the stability and growth of the U.S. domestic economy, as well as to world trade and political developments, makes it imperative that we thoroughly understand the problems and constantly reappraise the improvement programs involved. To this end, the Subcommittee on Inter-American Economic Relationships held (May 1962) two roundtable discussions: One, with specialists in Latin American agriculture, taxation, and labor; the second with representatives of firms with long South American investment and business experience.

These hearings were held for the express purpose of supplementing the subcommittee's previous study and the subcommittee's report¹ based upon an extended series of conferences held in South America last fall. This summary comment, while founded primarily upon the roundtable hearings, draws upon our continuing study. It is by no means a substitute for study of the transcript of the recent brief hearings but is intended only to highlight some of the thought-provoking issues brought out by the witnesses.

I. THE FLIGHT OF LOCAL CAPITAL

The testimony brought disturbing evidence of a reluctance on the part of some wealthy Latin American investors to risk private investment in their own countries. This reluctance is, indeed, reported to have taken the form of a substantial "flight" of local capital to Europe or the United States. Estimates presented to the subcommittee of the amount of this expatriated "flight" capital ranged from \$5 to \$15 billion. The \$10 billion estimate ascribed to one Latin American Minister of Economics is probably as good a figure to use as any.

The very nature of these fugitive funds makes it impossible accurately to estimate the amount of Latin American private holdings abroad. While short-term liabilities to Latin Americans, reported by banks in the United States, have held fairly constant, around \$2.5 billion, for the past 5 years, this is admittedly only a fraction of liquid Latin American assets in this country alone. There are no figures at all on foreign assets, including those beneficially owned by Latin American nationals, in Switzerland, and quite unreliable data about holdings in other countries of potential refuge. Year-to-year movements are, moreover, obscured by known omissions in the balance-of-payments statements—so-called "unrecorded transactions"—and by the certainty that undercover channels for escape will be sought out, and doubtless found, for capital illegally obtained or moving in defiance of exchange controls.

¹ "Economic Policies and Programs in South America," report of the Subcommittee on Inter-American Economic Relationships to the Joint Economic Committee (87th Cong., 2d sess.), January 1962.

Whatever the amount is, it is making the task of the Alliance for Progress more difficult. If substantial and persistent, it poses a serious threat to the ultimate success of the Alliance on which the very destiny of the Latin American investor class itself depends, and in which the United States, of course, is vitally concerned.

Though there is a tendency in many places to view the Alliance program chiefly in terms of expected grants and loans by the United States, the Alliance clearly calls for reforms and self-help on the part of the Latin American governments themselves. There is, moreover, the explicit expectation of sizable and growing private investment by domestic savers and capitalists, as well as by private foreign sources in Western Europe, Canada, Japan, in addition to the United States.

If local capital patently manifests a lack of faith in the prospects for its own domestic economy, the outlook for a substantial inflow of this essential private investment from outside is thereby discouraged and its amount inevitably lessened. The U.S. Government—and U.S. taxpayers—can hardly be expected to take kindly to any suggestion that it pour in, through added grants and loans, the funds needed to fill a capital gap created by the unwillingness and indifference of the financially able Latin Americans. This is especially so since uncooperative behavior locally is bound, by example, to compound the problem of attracting foreign private capital from all sources.

What, specifically, can the Alliance and the Alliance countries then do about this "flight" and voluntary exile of native capital—so obviously in conflict with the self-help programs and the hopes for development subscribed to at the Punta del Este Conference? First and foremost would, of course, be removal of the causes which prompt Latin American investment capital to leave home. The list of causes would undoubtedly include (1) fear of inflation, (2) fear of political and social instability, (3) risks of expropriation, as well as (4) relative unattractiveness, economically, of recognized investment opportunities. A moment's pause will show how intimately interrelated these factors are, if, indeed, they are not merely aspects of essentially one and the same condition.

Ironically, the causes of the private-capital flight which threaten the Alliance for Progress are precisely the things for which the Alliance, if given an opportunity to succeed, offers the best hope of cure.

The political instability of a middle-of-the-road government, when it tries to halt an inflation which has gone on for a number of years at a rapid rate, was noted in our earlier report.² Austerity measures, by stemming the rise in prices and wages, reducing swollen governmental expenditures, and easing exchange controls are certain, for a time, to alter the relative economic position of certain groups while improving the lot of others. Instability and uncertainty are not infrequently fed by governmental acts expropriating the property of nonresidents or, punitively, that of local residents currently in political disfavor. Sooner or later the inevitable recognition comes that expropriation has added nothing to total national wealth-in-being, has added little to economic or social welfare, but has succeeded only in adding further deterrents to investment, especially by private foreign sources.

Can a well-intentioned government stay in power long enough to survive changes designed to improve the climate for investment and

² "Economic Policies and Programs in South America," *ibid.*, p. 35.

allay the fears of instability? Can the less-well-intentioned government stay long in power if it yields, on the other hand, to the temptations of inflation and expropriation as ways of life? The record of the past in Latin America prompts one to a reluctant "no" answer to both questions. That has left us with the Gordian knot uncut, social unrest, overthrow of a precariously balanced government, more inflation, a new wave of expropriation, a worsened climate for private investment, still more social unrest. Only the determination and actions of the countries themselves—and that means those in political and economic power—can break the circle. The discipline and self-help contemplated by the Alliance, by ending the old pattern, offer the best hope of stopping the flight of domestic capital and, going beyond that, in attracting external capital in increasing amounts.

As to what else can be done to stop the reported flight of capital, other than remove basic causes, witnesses at the hearing mentioned two possible measures, but the success of even these hinges on acceptance of new patterns of thinking. Most of the Latin-American countries, we were told, follow the rule that only income arising from sources within the country is subject to taxation.³ Earnings on investments outside a country are thus free of tax, even though the owner is a citizen and resident. Such a policy seems almost to have been designed to enhance the attractiveness of investing outside the country. Granted that there are difficulties associated with an extraterritorial tax, the reforms now in progress as part of the Alliance "package" might consider taxation of income of residents or nationals, from wherever derived, accompanied by credit for taxes paid in the foreign country. That, at least, would remove the present premium in favor of expatriation. If enforced, it would lead to some knowledge of the amounts actually invested abroad.

It was suggested also to the subcommittee that the countries which have lost substantial amounts of domestic capital might give consideration to holding out the enticing "carrot" of amnesty to encourage return.⁴ By assuring investors that no questions will be asked about the "hows and wherefores" of the original flight, some of these capital funds might be repatriated just as some countries by amnesty have, on occasion, attracted gold out of mattresses and from under floorboards. Amnesty would be especially recommended if it resulted, as it well might, in bringing back home some of the native talent and personal skills which so often are lost through migration of persons along with the flight of capital. Amnesty must, of course, be so tempered that loyal, "stayed at home" money will not be discriminated against relatively.

On such alleviating proposals our subcommittee makes no recommendations. The testimony of one subcommittee witness seems, however, to sum up the priorities particularly well. It should provoke some thinking of the longer view on the part of the Latin American moneyed classes. He said:

I have the strong impression that ultimately the repatriation of such capital depends a good deal upon the initial success of the Alliance for Progress. If the program is in fact successful in building social improvements and developing the early stages of economic growth at an accelerated rate, you will find that capital

³ See hearings, "Economic Developments in South America," Subcommittee on Inter-American Economic Relationships of the Joint Economic Committee, May 10 and 11, 1962, pp. 31-32.

⁴ Hearings, *ibid.*, p. 32.

will be returning, because there will be an easing of the threat of upheaval, of totalitarianism. And it will be returning because in an expanding economy there will be new areas in which investment will be profitable.

And I would hope that at the time of return it would be a useful force for maintaining momentum initially built up by infusions of social capital, so to speak, in the Alliance for Progress.⁵

II. EFFECTIVE LOCAL GOVERNMENTS AND THE REAL ESTATE TAX

The hearings brought out again the general absence of effective local government instrumentalities in most of the South American countries. We were impressed on our visit to South America, and again from the testimony at these hearings, that the traditionally minor role assigned to local governments has been a dampening force on economic and social development.

Here in the United States we are, of course, quite accustomed to a division of responsibilities between the central Federal Government and the States and local municipal governments. The South American heritage, in contrast, has apparently never given a great role to these subdivision governments. The pattern has been, rather, one of the central government collecting the taxes, apportioning expenditures, setting priorities, and what was especially stultifying, providing the intellectual leadership, thereby deadening the energies and downgrading the abilities of potential local leaders. This has tended to leave local communities with little autonomy, little leadership, and resignedly dependent upon the central government for financial support and planning.

A government—even a well-meaning elite government—in a far away national capital is not ordinarily the best means of public capital formation. Self-help would, we believe, be encouraged by an expanding interest in planning and management of local projects where the potential taxpayers were able to see for themselves any sacrifices translated into recognizable local benefits. The prevailing pattern, calling for tax sacrifices without one's being able to see the benefits, gives rise to the notion that the national government swallows up everything, thereby increasing enforcement problems. The experts say, not unreasonably, that this feeling would be less of a dead hand on economic and social development if greater reliance were placed on a local source of revenue as the basis for needed local improvements.

Happily, the development of local government, largely absent up until now, has available a potentially healthy, relatively untapped source of revenue in the fact that a tax on property values has never been an important part of the Latin American tax system. This is in contrast to the familiar pattern in the United States where the property tax has been the backbone of local government activities in the support of schools, roads, police, sanitary facilities, and the like. Whereas in the United States, about one-sixth of all taxes are property taxes administered at the local level, it is estimated that property taxes, speaking generally of South America, amount to no more than 3 to 5 percent of all governmental income.

While not precisely on the issue of intergovernmental relationships, the heavy reliance of Latin American countries on sales and excise taxes (including customs) was called to the subcommittee's attention.

⁵ Hearings, *ibid.*, pp. 36-37.

In the United States, the "tax mix," including all levels of governments, is approximately two-thirds income taxes, one-sixth sales and excise taxes, and one-sixth ad valorem property taxes. In the countries of Latin America the "mix" more generally approximates 70 to 75 percent sales taxes, excise taxes, and customs duties; 20 to 25 percent income taxes; and 0 to 10 percent property and other capital taxes.

The failure to develop local property taxation has, it appears, been a deterrent in Latin America to the development of the usual supporting facilities—the infrastructure now recognized as prerequisite to economic growth, improved social conditions, and political stability. As one of the witnesses expressed it, the local property tax has a virtue far beyond its revenue-producing capacities; one of its greatest virtues is that it "forces communities to have a school board," a police commission, a water commission, a board of sanitation, which in turn make for local assessment of taxes and local formulation of considered plans for spending. By providing the financial resources with which to service interest charges and amortize principal, a local tax system would, moreover, permit the issuance of local improvement bonds and hence the longer run planning of such facilities.

A system of real estate taxation can, moreover, be an effective instrument for agrarian reform. A real property tax upon intrinsic values based upon location, use, and improvements tends automatically to bring about not only fairness but also an improved economic usage. By impelling absentee landlords to seek the highest economic uses for their land, it makes artificially administrative standards and enforcement of land use unnecessary.

From the evidence before us it seems that the Alliance for Progress might well give considerable emphasis to the development of local and provincial governments, and encourage use of local property taxes as a means for bringing about the educational and social development which is obviously the first need in these countries. Since property taxes have been so little used, but from experience in the United States appear to be one of the soundest sources of revenue, our impression would be that meeting the need for schools, access roads, and other infrastructure might well look to the capabilities of local and provincial governments. They offer not only financial media but have the added merit over central government taxes and loans of encouraging local initiative and self-development.

III. THE TECHNIQUE OF THE PUBLIC AUTHORITY

The technique of the public authority with mixed public and private attributes such as our port authorities, turnpike authorities, and multi-purpose valley authorities, or the Port of London Authority, was suggested as a potentially useful device for the kinds of development called for in Latin America. It provides a managerial device for dealing with a specific problem, housing, land reform, or the like; is especially adapted to local or regional projects, e.g., northeast Brazil; and "avoids vast encrustations of bureaucracy" which are likely to characterize remote control by the Central Government. It could "attract, for the top management, nonpolitical figures" and the "highly trained younger generation of technicians throughout Latin America" who at the present time "lack the power of political decision." With its more

precise and limited aims it would offer, too, some measure of isolation from the investment vicissitudes of national political instability.

It has merit, moreover, as a businesslike financing device, recommended by its limited and manageable proportions, even though its immediate ability to attract funds might necessarily lean heavily on Central Government or Alliance guarantee. It was suggested, for example, that creation of a public authority might in many cases forestall the urge toward expropriation, since many property owners would be willing to sell to a governmental project if given assurance that compensation was bound-up with a specific project and not merely government "wallpaper." The reported success of regional authorities where they have been tried in Latin America would seem to commend the technique as particularly useful in the development program.

IV. THE PRESSURES FOR LAND REFORM

The meaning and objectives of "agrarian reform" in the context of the Alliance for Progress, especially the interest and role of the U.S. Government as a participant in the Alliance, has tended to become confused as simply a tenure problem, but, properly conceived, should have as its primary objective increased agricultural productivity by a variety of means.

We in the United States are likely to hear emphasized, and hence come to think of the program as certainly some in Latin America do, as essentially one of breaking up large landholdings, or, in the words of the charter of Punta del Este itself, "replacing latifundia" by an improved owner-operated pattern of land tenure. This emphasis seems somehow to run counter to our own agricultural experience in recent decades when we have seen inefficient small holdings being combined, in the interests of increased productivity, into larger and larger units. Thoughtful persons in the United States are a bit uneasy, moreover, that the objectives of "agrarian reform" are punitively directed and that we are lending our tacit support, if not encouragement, to a program whereby property rights under law are being interfered with.

In our earlier report we listed a number of principles which it seemed to us should underlie programs of land reform. We would emphasize several of these by noting again that:

1. The primary objective of agrarian reform measures should at all times be increased agricultural productivity, recognizing that equity and a free democratic pattern of landownership may often be substantial contributors to that end.
2. Land reform thus is not exclusively a tenure problem but a problem of improved farming practices generally.
3. The major step in improving farming practices must come through rural education, research, and extension services aimed at improving such things as breeds, seeds, storage, and marketing.
4. Especially designed credit institutions to serve the production and landownership needs of local farming are likewise integral parts of productivity reform.
5. Land reform would include real estate tax reform, since a good real estate tax system is the cornerstone of land use and the corrective of underutilization, bad practices, inadequate local revenues to support the government facilities basic to local development.⁶

⁶ "Economic Policies and Programs in South America," *ibid.*, p. 24.

An extended excerpt from our recent hearings may help North Americans better to understand the agrarian "reform" problem and why it seems always to be placed so high on the Latin American agenda for progress. We were told:

To the campesino, ownership of land is more than a source of wealth. It is the source of prestige and political power and social justice. It gives him the right to build a school. It lets him share in the bundle of rights which have so long been a prerogative of the large landholder and denied to the landless.

The pressure for land reform, then, must be seen for what it is—pressure for a major reform in the government, the society, and the economy. Peaceful or violent, it is nothing more or less than a revolutionary movement.

We might well ask ourselves what specific expectations the landless of Latin America have from land reform.

1. *Economic security.*—Of course, the landless see in the ownership of a piece of land a kind of job protection and assurance that, whatever happens, they will at least have food and shelter.

2. *Political and social justice.*—Through landownership the landless hope for status in their communities, freedom to act and speak freely, the opportunity to see their children given an education, and the right to share in control over their government.⁷

Attesting the reality of some of these general observations is the report that in Bolivia a major effort at tax reform includes a proposal to tax land distributed to farmers under the Land Reform Act of 1956 and that the farmers have been glad to pay the tax, if for no other reason than that it proves that they really own the land.

This observation on the pressures for land reform, suggesting as it does the relationships of a quasi-feudal society, does not necessarily point to the wisdom of breaking up existing private estates as the necessary and only solution. Granted that the landless peasant may see, and perhaps find, in the ownership of a piece of property satisfaction of a long-felt need for security, prestige, and justice, these advantages can be found equally well through the distribution of government-owned public lands, under programs similar to our homesteading acts encouraging pioneers. To the extent possible, one of the first steps in land reform should thus be to bring together potential settlers and these undeveloped public lands suitable for cultivating.

Because of different temperaments of the populations, homesteading of Latin American public lands may not be as swift or eagerly grasped as in the United States in the 19th century. While we take justifiable pride in the heritage of our own pioneering ancestors who succeeded in conquering a continent in little more than 100 years, we cannot brush aside the physical and psychological reluctance of, for example, the Peruvian Indian, who, after generations in the highlands, may be incapable and unwilling to readjust to lower altitudes or distant provinces.

In summary, the pressures and measures for land reform are varied and mixed. The primary objective must be increased agricultural productivity, be it in the public lands or in uneconomically operated large private holdings. Education, research, and extension services are obvious channels of effort, since the basic problem is not only efficient use of the land, but of cultivating a pioneering spirit and capitalizing on the innate drives for ownership and possession.

⁷ Hearings, *ibid.*, pp. 14-16.

V. THE IMPORTANCE OF MANAGERIAL TECHNIQUES AND KNOW-HOW

Economic progress in Latin America needs a great deal more than capital loans and grants. The objectives of the Alliance may, indeed, be equally well advanced by the free "importation" from the industrial countries of capital-saving and efficiency-improving techniques and managerial know-how which, coupled with private investment, have made the flow of products from our enterprise system the envy of the world.

Nor are the techniques for improved capital productivity necessarily monumental or limited, for example, to the prototype automated steel mill which seems so often to be given high priority in the development plans for underdeveloped countries. Many of the capital efficiency devices are relatively minor business procedures such as we have come to take for granted. Together, they can make up a sizable package effectively substituting for capital and financial grants. The infinite variety and need for businessmen and "planners" alike to be on the "lookout" for capital-saving techniques, even though seemingly small in themselves, was dramatically brought to the subcommittee's attention by the testimony of a representative of the conspicuously successful Latin American operation by a U.S. company.

Perhaps, however, the record should first be made clear on one point, since it is itself an aspect of the type of managerial techniques in question. Although this particular company's name is a household word in the United States, its Latin American operations are by no means "Yankee." U.S. stateside personnel assigned to Latin America have been progressively reduced as the operations have grown until they now number only 45 out of over 5,000 employees. In several of the countries where the company operates, more than 98 percent of the merchandise purchased for resale, along with fixtures and equipment, are, moreover, purchased and produced locally. The "importation" of job opportunities and business procedure have thus effectively substituted for what might otherwise have called for substantial employment-building governmental grants.

Illustrative of these often taken-for-granted procedures, the witness mentioned as innovations in Latin America "merchandise contracting which enable the supplier to plan his production in order to lower his costs"; "selling methods typical of our U.S. stores such as fixed [ticketed] prices, out-of-store selling, cash handling by sales personnel, and extension of consumer credit." He went on to observe:

Every day that passes provides additional proof that we can and should apply the same criteria to our Latin American operations that we apply to our stores in the United States of America; high turnover at a reasonable markup; adequate sales per square foot of floor area; selling cost of sales personnel; commission rates; total payroll; advertising expenditures; return on advertising. These techniques, together with those involving sales promotion, are being passed on to our South American executives, and, in turn, are being copied by our competitors. The result, the establishment of a new and respected profession, that of the retail salesman and retail executive.³

The practice of fixed (ticketed) prices, and the direct handling of cash—instead of cumbersome, hand-itemized, handwritten sales slips, conveyed manually to a more or less remote cashier for making change and stamping to be returned to the salesman before wrapping can begin—are so accepted in U.S. practices that those who have not

³ Hearings, *ibid.*, p. 80.

experienced Latin America can scarcely understand why they are worth mentioning.

Nevertheless, such efficiency measures which are ordinarily associated with and certain to accompany American private enterprise abroad cannot be lightly dismissed. They, too, contribute in advancing the social and economic objectives of the Alliance of a better life for larger numbers. We mention them as examples of an infinite variety of measures deserving some of the attention which now tends to emphasize money grants and loans as a cure-all.

VI. THE NEED FOR HOUSING AND DOMESTIC SAVINGS

Since the capital for meeting housing needs alone could use up several times the total amount of funds contemplated under the Alliance for Progress for all purposes, it is obvious that the great bulk of the additional capital required for new housing will have to come from savings within the countries.

Both the Act of Bogotá and the Alliance for Progress stress the importance of meeting the desperate need for low-cost homes for low-income families as essential to social and economic advancement. The dimensions of the estimates of these housing needs are staggering. It is estimated, for example, that to replace the lowest one-quarter of existing urban housing—which does not go very far up the scale toward minimum adequacy—would require from \$10 to \$30 billion.⁹ If rural housing is also to be brought up to even the most modest of acceptable standards, this amount might well have to be doubled.¹⁰

In addition to taking care of these existing housing needs, both urban and rural, there is the problem of providing adequate low-cost housing to keep up with population growth—estimated to require a million units a year.¹¹ To provide for population increases and at the same time to make any substantial progress toward eliminating existing deficiencies in urban housing alone, it is estimated will take nearly \$4 billion a year. This is about double the current rate of home-building.

But how to get this new investment? The Act of Bogotá calls for a strengthening of the existing legal and institutional framework for mobilizing financial resources to provide better housing. It suggests that special consideration be given the existing legislation and measures:

- (a) Private financing institutions, such as building and loan associations;
- (b) Institutions to insure sound housing loans against loss;
- (c) Institutions to serve as a secondary market for home mortgages;
- (d) Institutions to provide financial assistance to local communities for the development of facilities such as water supply, sanitation, and other public works.

In a symposium paper by one of the witnesses included in the hearing record, an interesting suggestion is made for setting up an international housing finance institution to assist in the mobilizing of local

⁹ Hearings, *ibid.*, pp. 69-74.

¹⁰ See, for example, the estimates of rural housing deficiencies in Peru and Venezuela in "Social Progress Trust Fund," First Annual Report, 1961, Inter-American Development Bank, June 1961, pp. 192 and 215.

¹¹ Hearings, *ibid.*, p. 70.

savings for housing investment. This proposal deserves study and consideration. It was suggested that such an institution might usefully be a part of the Inter-American Development Bank or a subsidiary of that Bank:

This housing association would have three functions:

- (1) It would set standards for housing construction and financing, with due appreciation of differences in local conditions;
- (2) It would insure for a fee, approved mortgage loans up to a percentage of their face value, though the lender would have to take at least 10 percent and perhaps more of the risk;
- (3) It would develop a secondary market in insured mortgages to smooth out short-term swings in the flows of mortgage money and increase the liquidity of mortgage investment.

A program would have to be worked out for local participation in the Latin American Housing Association. In general, commercial banks, insurance companies, other private savings institutions, and perhaps even Government pension funds could qualify by agreeing to observe certain standards in mortgage lending and perhaps by purchasing a small amount of stock in the Association. They could originate mortgages which the Association would guarantee if its standards were met. The problem of inflation would have to be faced—through local government exchange guarantees and escalator clauses, or more hopefully, through measures to contain inflationary pressures.

The capital of the Latin American Housing Association would be supplied by the members of the Inter-American Development Bank, plus any subscriptions from participating mortgage lending institutions. Its income from mortgage insurance fees could be set to cover losses over a period of time.¹²

Other testimony suggested that long-term funds from the United States to invest in foreign mortgages arising from low-cost housing projects might be stimulated by improving the all-risk guarantees of the Act for International Development of 1961. The present requirement covers an undivided 75 percent of the exposure. The 25-percent risk that is not guaranteed prevents fiduciary funds such as labor welfare funds from investing. Without these guarantees, it seems unlikely that there would be anything other than a trickle of private capital from abroad. But even with their help, the great need will still be for local funds.

The housing problem is of such dimensions and such diversity, or course, that no single solution will suffice. Subsidy and direct governmental help will be needed for the lowest income groups in city slums.

The self-help projects, both urban and rural, may well be a way of stretching housing funds where labor is abundant and materials scarce. As the financing problems are being resolved, the housing industry and various national institutions can contribute to improving the house itself by developing better standards, by training craftsmen, and by research in new methods and materials.

VII. THE DILEMMA PRESENTED BY DEPENDENCE UPON LIMITED EXPORT COMMODITIES

General price inflation is the lot of almost any country with a measure of monetary or fiscal mismanagement but the fate of a country dependent, as most of the Latin American countries are, upon one or two export commodities, is subject to an ever-present added complication. For them, changes in one or two specific prices may mean economic difficulties, political unrest, and thwart economic development. Worse yet, these prices are likely to be less susceptible to even good local management since they are world prices in a world market.

¹² Hearings, *ibid.*, p. 73.

The implications of the commodity problem to Latin America were dramatically illustrated in one instance cited to the subcommittee at its recent hearings. In Colombia alone, despite generous assistance in the way of credits for both economic development and social welfare, "the losses suffered in the coffee market and prices since the Punta del Este Conference are two or three times greater than the special aid received."¹³

Success of the Alliance for Progress depends, one must conclude, in large measure upon finding a satisfactory solution to the problems arising out of this extreme dependence on a few primary products to provide large segments of domestic employment and earn the foreign exchange needed for economic progress and development.

The commodity problem, however, presents unhappy dilemmas for all parties.

(A) For the Latin Americans themselves, the questions arise, (1) Dare we hope and wait for diversification, and what can be done to speed it? (2) Or must we rely, we would hope transitionally, on uncertain and uneconomic price support and quota programs even though these be given the support of consuming countries?

(B) As a matter of U.S. policy, the questions may well be asked, (1) Do we undertake "to pump" into Latin America under the Alliance a billion dollars annually which, in recent months, has not even been sufficient to close the export-import gap experienced by some of our friends in the development effort? (2) Or, alternatively, must we commit ourselves to participation in commodity price stabilization agreements, the cost of which may be staggering, which experience suggests may prove to be of little success, and which may rouse the resistance of American consumers to higher prices; e.g., coffee?

(C) Other countries in the Western World, presumably as concerned as those in the two continents of America, are in holding back the Communist threat, might well be asking themselves, (1) Is it really smart policy for us, by common import restrictions and domestic subsidies, to be fostering relatively inefficient national production of selected agricultural products such as sugar and meat if we thereby add to the difficulties of the underdeveloped countries which are today crying for an opportunity to progress? (2) Does it really serve our overriding interest to lean heavily for domestic tax revenues on high excises and import duties on products such as coffee, cocoa, and bananas, when exports of such products are so overwhelmingly important in determining the economy and welfare of friendly developing allies?

The subcommittee has no ready answers to any of these questions. Their asking nevertheless shows something of the task ahead for everybody if the Alliance for Progress is to succeed.

While we may justifiably have little taste for international cartel agreements, we cannot push under the rug the threat to success of the Alliance posed by commodity fluctuations which are capable, within a matter of months or a year, of wiping out a country's foreign hard-currency earnings. We noted also in our earlier report the transitional problem tempting the Latin American nations themselves to undertake essentially uneconomic production. From their short-run standpoints, the easiest way to increase exports would be to

¹³ Hearings, *ibid.*, pp. 51-52, 87.

concentrate on the production of the commodity in which their natural advantage is already established. But this has the drawback of increasing their already too great dependence upon these commodities. The need is for increased exports but also to diversify these exports.

During our hearings several possibilities that might mitigate or make it easier to live with the commodity problem were brought to the attention of the subcommittee. Perhaps the encouragement of "future markets" would help. Perhaps an international agreement, providing that in case a nation's commodity export earnings decline more than a specified percentage, part of the shrinkage might be made up by international loans, would offer a measure of relief. Perhaps, recognizing full well that the law of supply and demand, even in the hands of government, seems to work inexorably as a short-term mechanism, we may still have to depend upon buffer stocks or quotas.

The efforts of the Latin American governments to solve the many-faceted commodity problem will call for great ingenuity on their part as well as the trade cooperation and sympathetic understanding of the United States and the other free world countries.

VIII. DEPENDENCE OF THE ALLIANCE FOR PROGRESS ON DEVELOPMENT OF EFFECTIVE CIVIL SERVICE SYSTEMS

One of the considerations to be taken into account in judging the speed and momentum of the Alliance for Progress is the fact that very few Latin American countries have a true civil service. Our own observations in South America were confirmed by the testimony of the experts, suggesting that—

it is not feasible to carry out an economic plan at the national level without a sufficient number of qualified technicians adequately organized and secure in their tenure. At best it will take years to create a responsible and efficient public administration but this aim should be very close to the top of the agenda of the Alliance.¹⁴

We noted in our earlier report that in development planning it is best not to rely too heavily on government as opposed to the private sector to accomplish economic achievements even though one is forced to recognize at the same time that many of the immediate needs for plans, surveys, and action are concentrated in the public sector, such as education, transport, and energy. The true career service in most of the Latin American countries as measured by special training and security of tenure has traditionally been "the military." The significant thing for our thinking is the need for first extending governmental career service into civilian fields. While this is a prerequisite to the long-term objectives of the Alliance, it is likely to make for a seemingly slow start in terms of ultimate objectives.

A variety of other institutional reforms, such as adequate statistics and basic education, are likewise prerequisite to effective reform and growth. The need for first developing tools and instruments suggests that the goals of the Alliance for Progress in overcoming years of neglect may not be fully remedied in a single decade. While the decade target is useful in stressing urgency, the vastness of the needs and the basic changes called for may even now be recognized as problems of a generation or perhaps longer.

¹⁴ Hearings, *ibid.*, p. 22.