In this chapter an attempt is made to analyse the nature of the foreign trade problem faced by the developing economies and to state the main lines on which policy should be formulated. In section I we discuss the role of trade in development. In the period before the second world war foreign trade played the part of an engine of exploitation in most of the developing countries of the present. The circumstances responsible for this development are analysed and it is stressed that foreign trade should be made to play the role of an engine of growth. In the next two sections we analyse the present position of foreign trade in these countries. The main problem is that of mounting imports on the one hand and slow growing exports on the other. A related problem is that of adverse terms of trade. It is in the light of these problems that we take up, in the last section, the question of trade policy. Imports are bound to be high for a long time to come, but there is scope for import saving and import substitution. The diversification of both production and export should get top priority and export promotion should be incorporated with the strategy of development. These necessitate restraints on consumption and the stepping up of investments. The problem, in short, is ultimately that of striking the proper balance between investment, domestic consumption and exports. The realisation of this objective may be regarded as the central problem of commercial policy.
ROLE OF FOREIGN TRADE IN DEVELOPMENT

The Chapter in the Wealth of Nations in which Adam Smith deals with the "Mercantile System" contains a point-by-point refutation of the system of national self-sufficiency advocated by the Mercantilists. The Nineteenth Century saw the triumph of the principle of economic liberalism and a phenomenal increase in the volume of world trade. Thus in the period before the first world war one-sixth of world production entered into international trade and between 1850 and 1880 there was a 270 percent increase in the volume of world trade.¹ Foreign trade also became an "engine of growth"² as it was through foreign trade that countries like the U.K. accumulated the capital required for industrial development.³ Economic growth was thus speeded up in the U.K. and a few other countries, but the resulting demand for raw materials and food led to the transmission of growth to a number of other countries. The principle of international division of labour, so forcefully presented by Adam Smith had apparently proved correct.

The process of growth-transmission through increased demand for raw materials and food and a steadily increasing outflow of capital for investment purposes mainly benefited the "new countries":

¹. Ragnar Nurkse. Patterns of Trade and Development.
³. "In England at the time of Ricardo the margin of cultivation was creeping up the hillsides into poorer and poorer land and it is clear that without the burst of external trade which occurred soon afterwards, the struggle for food would have prevented industrialisation from going as far as it did in Britain and elsewhere in Western Europe". Ragnar Nurkse. Op-cit.
The "exotic countries" like China, India and the countries of tropical Africa and Central America benefited much less. These are the most underdeveloped regions of the present day. In their case the European contact generally resulted in the creation of "dual economies" in which well-developed export sectors co-existed with backward internal economic conditions. The export sectors were usually developed by foreign interests and to some extent by local groups. Thus both foreign capital and local capital flowed into the profitable export sector which catered to the requirements of colonial nations which, in return, supplied manufactured articles. The colonies were discouraged and even prevented from developing manufacturing activities. Thus a few colonial powers were able to grow richer at the cost of their colonies. The resulting position was that "the United States, Great Britain, France and Germany, representing 13 per cent of the world's population, owned almost 50 per cent of the world's goods, and more than two-third of the world's income was reserved for less than one-third of the world's population". Under these circumstances the backward nations denounced liberalism and viewed foreign trade as an engine of exploitation. This fact has to be appreciated in interpreting the approach of the underdeveloped countries to problems of foreign trade.

The United Kingdom who championed the policy of economic liberalism soon began losing faith in it and started adopting restrictionist policies. The fears of the under-developed regions were thus confirmed. This process commenced towards the close of

4. Ragnar Nurkse, Ibid.
the nineteenth century. Germany and the U.S.A. had industrialised themselves behind tariff walls and the U.K. relaxed her liberal policy. The first world war, the economic depression of the thirties and the second world war further strengthened economic nationalism, with the result that the nineteenth century pattern of trade collapsed under the combined weight of these factors. A steady decline in the proportion of production entering world trade was the result. According to Prof. Murase the volume of world trade increased by 270 per cent between 1850 and 1880, while between 1880 and 1913 the increase was only by 170 per cent and between 1928 and 1958 by only 57 per cent.

TRADE AND GROWTH:

We may now consider the factors responsible for preventing foreign trade from becoming an engine of growth in the underdeveloped countries. The expansion of foreign trade was the first stage in the economic development of countries like the U.K. and Japan. It was through foreign trade that these countries raised their savings and investments. In the case of the U.K. the main export commodities were wool in the period before the industrial revolution and cotton textiles during the early stages of the industrial revolution. In the case of Japan the commodity was silk. Through these exports the U.K. and Japan achieved the stage of self-sustained growth in their economies. In contrast we find that in countries which came

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6. Ibid.
7. During the crucial period of development silk provided most of the foreign exchange required to pay for equipment imports. Total exports increased from an average of 16 million Yen in 1868-1878 to 2434 million Yen during 1914-1920. During the same periods imports increased from 23 million Yen to 13000 million Yen. G.C. Allen. A Short Economic History of Modern Japan, 1868 - 1937.
under the political and economic domination of western colonial powers the development of foreign trade did not initiate a process of economic growth. A few advantages did flow from the development of foreign trade, but on the whole foreign trade on a larger scale only disrupted the economic balance and failed to introduce a new balance. An investigation of the causes responsible for this state of affairs throws light on some features of colonial economies.

Haberler\(^8\) points out that if international trade enables a country to produce cheaper goods to exchange for what other countries can produce at a lower cost, such an exchange raises the level of income and also promotes economic development. This, however, was not the course of events in several countries including India which were under foreign domination. One factor responsible for this was that the effective demand generated by foreign trade did not remain within the exporting country, but "leaked abroad".\(^9\) The plantations and the few industries in the primary-producing countries were mostly under the control of foreigners who remitted business dividends and salary-savings to their own countries.\(^9\) Expenditure on capital goods incurred by the industries also benefited foreign countries as there were no capital goods industries in the primary-producing areas. These constituted a savings-leakage. There were also import leakages as there were few local industries and imported goods were cheaper and superior in quality. The free trade policy followed facilitated these imports and destroyed the existing traditional industries of the primary-producing areas. The result was that the expansion of the export sector had little influence on conditions in the home sector.\(^10\).

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Another explanation is that the international specialisation which occurred in the primary-exporting countries was not really conducive to cumulative improvements in technical skill and productivity, but led to "once-for-all increases in productivity accompanying the transfer of labour from the subsistence economy to the mines and plantations"\(^{11}\). In other words, once the initial investment of capital took place there was no subsequent capital-deepening investment and stagnation resulted. The initial improvement in productivity and output in the export sector was thus an isolated phenomenon. It did not spread to the domestic economy and forward linkages were exported and not retained within the country.

Another factor which limited the growth-spread effect of foreign trade was that though the primary-producing countries possessed various resources they were not in usable form. In other words the resources did not constitute factors of production or effective supply. Large populations, for instance, did not constitute effective supplies of labour in the absence of training. Land and mineral resources also lay undeveloped. Thus in the absence of resource development there was no possibility of the export sector influencing the home sector of the economy. The foreigners who controlled the economies of primary-producing countries were interested only in lines of activity which were of immediate benefit to themselves. Within the primary-producing countries there was neither the capital nor the technical knowledge required for resource development. The primary-producing countries thus had a 'dual economy' in which an organised, but not always dynamic, export sector co-existed with a positively stagnant domestic sector.

It is with reference to the facts of, and trends in, international trade discussed above that the approach of developing countries towards trade have to be studied. As victims of imperialism, both in its political aspect and in its economic aspect, these countries attached considerable importance to the achievement of economic independence. Thus even in 1948 the U.N. noted the existence in these countries of a definite tendency towards national economic independence, characterised by the desire for balanced economic development, and by the imposition of controls over trade, exchange and investment with a view to fostering such development. 12.

The desire for economic independence, however, does not imply the mere desire for balanced economic development. To the under-developed countries in general it has often meant minimum external economic contracts. It thus conflicts with the principle of specialisation which is the very basis of economic progress. Such a state of affairs in neither desirable nor even practicable except in cases where subsistence economies prevail. 13. The fact that the resources of the world are unequally distributed makes it essential that advantage should be taken of the principle of regional specialisation. 14. This actually stimulates economic development. Developing countries should, therefore, plan for larger foreign trade and give up the idea of economic independence.

13. "Contrary to certain idyllic notions, a subsistence economy is not one which is secure, in that it provides its members with a modest but assured living. Its risks are much greater than those of an exchange economy, since it usually operates on a very low level and is without reserves against adversity". P.T. Bauer. Is Economic Independence Desirable? - Commerce Annual Number 1960.
14. "The division of labour referred to is not only in its static sense when resources are given but also in the dynamic sense when the development of the potential human and material resources leads to the dynamic concept of comparative cost". M.S. Kān.: India's Economic Development and International Economic Relations.
Foreign trade has the supreme advantage that it enables a developing country to acquire the capital goods required for economic development. The developing countries themselves can produce capital goods only if they invest on a very large scale in resource development, both material and human. The development of technical skill is particularly difficult and is a time-consuming process. The production of capital goods within the developing countries can therefore, be viewed only as a long-term development. But the process of economic development could be speeded up with the help of foreign trade. It thus becomes possible to secure capital goods through imports, but in order to secure such imports it becomes essential to step up exports. The result is an increase in trade both ways.

Another point which has to be emphasised is that the developing countries generally have what have been called small economies. The implication is that their incomes and purchasing powers are extremely low. Thus the domestic markets of these countries are not large enough to provide adequate opportunities for the development of various lines of production. The world market thus assumes importance as a stimulus to economic development. Larger production, larger exports and larger imports may be depended upon to speed up economic growth.

Foreign trade is also the means of acquiring technical and managerial skill. This is no mean advantage to the developing nations.

15. "Their progress depends very much upon capital investment; their investment depends to a large extent upon imported capital goods; and their capacity to import those items depends upon their foreign trade". Raymond Frost, The Backward Society.
which are technologically backward. Technological progress, in fact, holds the key to the future development of these countries and by securing it to them in some measure foreign trade acts as a stimulus to development.

To sum up, foreign trade improves not only consumption welfare by making available to the consumers a wide variety of goods which are either not available within their countries or are available only at a high price. The classical economists emphasised only this aspect of international trade. Foreign trade is particularly valuable because it develops productive capacity. This happens directly as a result of imports of capital and producers' goods; indirectly it arises from the spread of technical knowledge and skill. These developments lead to increases in income and to the creation of demand for various goods. Development is thus stimulated not only in the export sectors but also in the non-export sectors. These cumulative developments in turn lead to more trade. Thus a country in the process of development finds itself increasingly dependent on trade with other countries.

The alternative method available to the developing countries is the Russian model of development under which everything possible was produced within the country and foreign trade was reduced to the minimum. Actually it was the continental character of both the U.S.S.R. and the U.S.A. that enabled those countries to attain a

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16. "Trade is no mere exchange of goods, least of all when it takes place between economies at different stages of development. As often as not, it is trade that gives birth to the urge to develop, the knowledge and experience that make development possible, and the means to accomplish it. A.K. Cairncross. Factors in Economic Development."
high degree of self-sufficiency. Such a situation does not exist in any other country. The developing countries should, therefore, evolve suitable foreign trade policies and incorporate them in their plans of development. It is also necessary to devise policies in order to induce the people to save more and consume less so that imports, particularly of avoidable articles, are kept at a minimum and exports are maximised, and what is thus withdrawn from consumption is converted into investments through the process of saving. Foreign trade has thus an important part to play in economic development and it will be in the interest of each developing country to formulate its own strategy of foreign trade and also work it out efficiently.

II.

SLOW GROWTH DEMAND FOR EXPORTS.

Export trade has, in the post Second World War period, assumed a new character. It is no longer a means of acquiring ordinary consumption goods and creating hoards of money. It is now the principal means to finance purchases of capital and production goods required for purposes of economic development. The developing countries have thus acquired a vested interest in increasing their exports. But their present pattern of exports is such that a fast enough increase in exports is often difficult. This arises from the fact that their exports are mostly based on the bounty of nature—that is, they generally export natural products, agricultural and mineral. In fact, as pointed out in the previous section the present pattern of exports was the result of deliberate policy on the part of the colonial powers. But in the post-war world, conditions have
so changed that the developing nations find that their existing pattern of exports is far from stable.

World trade figures published by the U.N. show that in the fifties the total exports of advanced countries increased about a hundred per cent, while the total exports of the developing countries increased by only 38 per cent (Table 2.1). This shows that there has been rapid economic recovery in the advanced countries in the post-war period, while the underdeveloped countries had to be content with slow progress. Several under-developed countries had actually built up large foreign exchange reserves during the war through large-scale exports of primary goods and hoped to utilise them for purposes of development. But economic trends during the immediate post-war years shattered these hopes and the reserves accumulated through reduction in consumption and other privations were practically frittered away by importing less-essential goods.17. The future prospects for the exports of the under-developed countries also appear to be far from bright. In fact, according to a U.N. survey the position is likely to worsen during the next few years.18. Certain mineral products alone

17. "The foreign exchange surpluses (mainly in dollars and sterling) accumulated during the war as a result of expanded exports of primary goods at a time when imports of industrial products could not be obtained, rapidly lost a substantial part of their purchasing power. At the very time that industrial products began to be available for export, prices in the U.S. rose 40 to 50 per cent following the end of price controls in the summer of 1946. The rise in industrial prices retro-actively deteriorated, to a considerable extent, the terms of trade between the wartime exports of the underdeveloped countries and their post-war imports. Considerable losses were thus inflicted on the economies of these countries, and the resources available for their development were substantially reduced." Paul Alpert. Economic Development.

seem to have a chance of being in great demand. But minerals of the required kind are not available in all underdeveloped countries. Generally these countries rely on exports of agricultural produce and specialisation in this direction has been carried too far in a number of them. Further, they generally have close trade and currency links with particular developed countries. Several years after acquiring political independence these countries still find it difficult to free themselves from these links. Thus changes in income and consumption patterns in their main markets, as well as differences in world demand for, and supply of, their staple export products produce serious repercussions on their export trade in particular and their economies in general. With schemes of rapid economic expansion on hand and the need for pushing exports further in order to acquire more imports the existing pattern of exports only creates instability.

The basic explanation for the present state of affairs is that agriculture is fast ceasing to be a firm foundation for the export trade of the underdeveloped countries. At present over one-half of world trade is carried on between the developed countries themselves. In 1962 trade between developing and developed nations was 30 per cent of the total and trade among developing nations about 5 per cent.

19. According to U.N. studies, there were, during the year 1960-61, 99 separate countries specialising in the export of one, two or three main groups of primary commodities. The term "specialisation" as used here denotes receipt of 50 per cent or more of export value. Thus 57 countries specialised in the export of one commodity group, 37 in two commodity groups and only 5 in three commodity groups. It is further noticed that there has been little change in this pattern over the past decade. Quoted by A. Maizels, Trade and Development Problems of the Under-Developed countries: The Back-Ground to the United Nations' Conference. National Institute Economic Review. No. 28. May 1964.
Over the past decade the value of exports from the developed countries rose about twice as fast as those from under-developed countries, the former by 77 per cent and the latter by 36 per cent. The value of trade between the manufacturing countries grew by 14 per cent between 1958 and 1959 and by 20 per cent in 1960, while the rate of growth of exports of primary producing countries to manufacturing countries lagged behind and remained static at 5 per cent during those years.\textsuperscript{20}

The industrial countries increased their exports not only in industrial goods but also in food and raw materials. Exports of food from the developed countries rose five times as fast as those from under-developed countries, while in the case of raw materials the rise was greater by two and a half times. In the case of food and raw materials together exports from the developed areas exceeded those from the under-developed areas by over 50 per cent in 1962.\textsuperscript{21} Further, a good part of the increased exports of the non-industrial countries is accounted for by exports from Australia, New Zealand and South Africa.\textsuperscript{22}

Table 2.1 brings out the main trends in world trade since 1928.

\textsuperscript{20} International Monetary Fund, Annual Report 1961. P. 52.
\textsuperscript{22} B.K. Rangnekar, India, Britain and European Common Market. Page 90.
Table 2.1

TRENDS IN EXPORTS FROM DEVELOPED AND UNDER-DEVELOPED AREAS

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
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<tr>
<td>Value</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Developed Areas</td>
<td>22.6</td>
<td>15.2</td>
<td>44.6</td>
<td>53.3</td>
<td>73.3</td>
<td>87.8</td>
<td>98.1</td>
</tr>
<tr>
<td>Under-developed Areas</td>
<td>9.1</td>
<td>5.9</td>
<td>21.6</td>
<td>21.3</td>
<td>25.2</td>
<td>27.5</td>
<td>30.4</td>
</tr>
<tr>
<td>Total</td>
<td>31.7</td>
<td>21.1</td>
<td>66.2</td>
<td>74.7</td>
<td>98.5</td>
<td>115.3</td>
<td>128.5</td>
</tr>
<tr>
<td>2 as P.C. of 3</td>
<td>28</td>
<td>28</td>
<td>33</td>
<td>28</td>
<td>26</td>
<td>24</td>
<td>24</td>
</tr>
</tbody>
</table>

Sources: 1. League of Nations, Review of World Trade.

CAUSES FOR DEMAND DEFICIENCY:

The causes responsible for the sagging demand for the exports of the under-developed countries have been analysed by Prof. Hursaka.23.

We now proceed to discuss those factors.

1. SYNTHETIC PRODUCTS: During the past few years synthetic producers have become great competitors to the exports of the under-developed countries. In 1952-'54 synthetics represented 9 per cent of the value...
of consumption of all industrial materials in the developed countries, while by 1960-1961 the proportion had risen to 15 per cent. The rate of growth in the consumption of synthetics has been four times as fast as the rate of growth in consumption of the various natural materials. In 1960-’61 the proportion of synthetics in the consumption of industrial materials was 49 per cent in Japan, 17 per cent in the U.S.A., 15 per cent in the U.K. and 14 per cent in continental West Europe. The export of synthetics from the developed countries to the rest of the world is also growing. The following table brings out the rapid progress of synthetics.

Table 2.2

CONSUMPTION OF SYNTHETIC MATERIAL PER HEAD
U.S. Level 1952-’54 = 100.

<table>
<thead>
<tr>
<th></th>
<th>1952-’54</th>
<th>1960-’61</th>
</tr>
</thead>
<tbody>
<tr>
<td>United States</td>
<td>100</td>
<td>161</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>46</td>
<td>107</td>
</tr>
<tr>
<td>E.E.C.</td>
<td>29</td>
<td>80</td>
</tr>
<tr>
<td>Other West Europe</td>
<td>10</td>
<td>37</td>
</tr>
<tr>
<td>Japan</td>
<td>21</td>
<td>91</td>
</tr>
</tbody>
</table>


2. LOW INCOME ELASTICITY OF DEMAND: The income effect is another important factor. In relation to foodstuffs it is an application of Engel’s law on the international plane. Thus a rise in the

level of income is accompanied by a fall in proportionate expenditure on imported foodstuffs. This phenomenon has already affected various exports of the underdeveloped countries.

3. AGRICULTURAL PROTECTIONISM: Another significant development is that during the past decade the greater part of the increase in consumption of agricultural produce in the developed countries was met by home production. One method adopted to achieve this was to invest on a large scale in improving the technology of agriculture. A policy of agricultural protectionism has also been adopted by the industrial countries. Farm support policies resulted in a greater expansion of food production than would otherwise have occurred.

Substitution is also making progress. For instance, cheaper animal fats are increasingly in use in place of vegetable oils in the making of soap and margarine. Again, the soya is becoming popular and is displacing coconut, ground-nut, cotton-seed and palm kernel oils.

It has been calculated that about 30 per cent of exports from the underdeveloped areas have now to compete with protected agricultural products in the developed countries.26.

4. ECONOMIES IN THE USE OF RAW MATERIALS: Another aspect of the substitution effect is the trend towards a lower quantum of material consumption per unit of output. This is a long-term trend and involves the development of new manufacturing techniques. The increasing use of materials previously wasted, the production of lighter products such as light-weight clothing, lighter-machines etc. and the increasing degree of fabrication of industrial products

are some of the practices. This may be regarded as a direct substitution of technology for raw material inputs. A notable example is the development of the electrolytic process of coating tin on steel sheets in the making of cans. According to a G.A.T.T. study the consumption of both natural and manufactured raw materials as a percentage of the gross value of manufacturing production in the industrial countries declined from 25.8 in 1938 to 20.7 in 1955.

5. CHANGING PATTERN OF INDUSTRIAL PRODUCTION: Yet another important development is the changing pattern of industrial production. Economic growth involves not merely an expansion in the total output of manufacturing, but also a structural shift in the pattern of output. Thus the composition of industrial production in the developed countries has been shifting away from "light" industries to "heavy" industries such as engineering and chemicals, or, in other words from industries which require a high percentage of raw materials to those which require less.

6. RISING SHARE OF SERVICES: Another factor mentioned by Prof. Murske is that the rising share of services in the total output of advanced industrial countries tends to cause their raw material demand to lag behind the rise in their national product.

All the above mentioned factors have adversely affected the exports of the underdeveloped countries. The consumption of natural rubber, textile fibres like cotton, wool and jute and hides and skins

have either declined or grown very slowly in developed countries. The demand for vegetable oils is also declining, while the demand for coffee and tea is static. The restrictionist policies which encourage home agriculture and industry affect both the agricultural and industrial exports of the developing countries. Thus during the so-called commodity slump period, i.e. 1955-'56 to 1961-'62 the foreign trade picture of the developing countries became particularly gloomy. The value of the combined exports of developing countries increased at about 2 per cent per annum, as against 6 to 7 per cent growth rate in the exports of the developed countries. The average rate of growth in exports was 2.9 per cent for Africa, 1.4 per cent for Asia and 0.9 per cent for Latin America. The distinctly higher rate for Africa reflects the demand for some of the products of that continent. Actually among the developing countries the export of the industrialising countries have been affected to a greater extent than those of others. When petroleum and related products are excluded it will be seen that the export trade position of the group of Asian countries classified as under developed is really serious. There has been improvement in the situation since 1963, but there is no indication that this will be anything but temporary. It will be more reasonable to regard the trend in world trade during the period 1948-1961 as a long-term phenomenon indicating what is in store for the under-developed countries for the next quarter of a century.
### Table 2-3

**WORLD TRADE BY COUNTRY GROUP**

(Millions of U.S. Dollars; Figures in Brackets are duties with 1948 Base as 100)

<table>
<thead>
<tr>
<th>Exporting country</th>
<th>1938</th>
<th>1948</th>
<th>1952-</th>
<th>1955-</th>
<th>1958-</th>
<th>1961-</th>
</tr>
</thead>
<tbody>
<tr>
<td>Group</td>
<td>(AV)</td>
<td>(AV)</td>
<td>(AV)</td>
<td>(AV)</td>
<td>(AV)</td>
<td>(AV)</td>
</tr>
<tr>
<td>World Total *</td>
<td>23500</td>
<td>57300</td>
<td>82500</td>
<td>102430</td>
<td>116733</td>
<td>133400</td>
</tr>
<tr>
<td>(41) (100) (144) (179) (204) (233)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Developed Countries *</td>
<td>15200</td>
<td>36500</td>
<td>53333</td>
<td>67500</td>
<td>77033</td>
<td>90200</td>
</tr>
<tr>
<td>(42) (100) (146) (185) (211) (247)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Developing Countries</td>
<td>5900</td>
<td>17100</td>
<td>21333</td>
<td>24667</td>
<td>25933</td>
<td>27600</td>
</tr>
<tr>
<td>(35) (100) (125) (144) (152) (161)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Centrally Planned</td>
<td>2380</td>
<td>3690</td>
<td>7843</td>
<td>10270</td>
<td>13767</td>
<td>15650</td>
</tr>
<tr>
<td>Economies</td>
<td>(65)</td>
<td>(100)</td>
<td>(213)</td>
<td>(278)</td>
<td>(373)</td>
<td>(424)</td>
</tr>
</tbody>
</table>

| Group                   | (AV)  | (AV)  | (AV)  | (AV)  | (AV)  | (AV)  |
| World Total *           | 25400 | 63400 | 86400 | 108333| 122867| 140200|
| (40) (100) (136) (171) (194) (221) |       |
| Developed Countries *   | 17900 | 41000 | 55567 | 71233 | 80166 | 93100 |
| (44) (100) (136) (174) (196) (227) |       |
| Developing Countries    | 5800  | 18600 | 22767 | 26800 | 28333 | 30700 |
| (31) (100) (128) (144) (152) (165) |       |
| Centrally Planned       | 1700  | 3800  | 7767  | 10300 | 14337 | 16400 |
| Economies               | (45)  | (100) | (204) | (271) | (378) | (431) |

* Trade between China, Mongolia, North Korea and N. Viet-Nam excluded.
• Includes Japan, Australia and New Zealand.

### Table 2.4

SHARE OF COUNTRY-GROUPS IN WORLD TRADE

(Percentage)

<table>
<thead>
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<tr>
<td>Total World</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td>Developed Countries</td>
<td>64.7</td>
<td>63.7</td>
<td>64.6</td>
<td>65.9</td>
<td>66.0</td>
<td>67.6</td>
</tr>
<tr>
<td>Developing Countries</td>
<td>25.1</td>
<td>29.8</td>
<td>25.8</td>
<td>24.1</td>
<td>22.2</td>
<td>20.7</td>
</tr>
<tr>
<td>Centrally Planned</td>
<td>10.1</td>
<td>6.4</td>
<td>9.5</td>
<td>10.0</td>
<td>11.8</td>
<td>11.7</td>
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<td>Economies</td>
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<tbody>
<tr>
<td>Total World</td>
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<td>Developed Countries</td>
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<td>65.2</td>
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<td>6.0</td>
<td>9.1</td>
<td>9.6</td>
<td>11.7</td>
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<tr>
<td>Economies</td>
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</tbody>
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Tables 2.3 and 2.4 give the trend of world trade during the period 1938 to 1961. During this period two stages may be noted.

Between 1938 and 1948 the exports of the world and of developing countries increased respectively by 144 per cent and 190 per cent.

But the exports of developed countries increased by only 140 per cent.
The share of developing countries in world exports increased from 25 per cent in 1958 to about 30 per cent in 1948, while the share of developed countries actually declined. The large demand for foodstuffs and raw materials of the war and immediate post-war periods was the main factor responsible for the export expansion of developing countries during this period.

The situation, however, distinctly changed between 1948 and 1961 when the exports of the world, of developed countries and of centrally planned economies increased by 133 per cent, 147 per cent and 324 per cent respectively. But the exports of developing countries registered poor growth. As Table 2.3 shows their exports increased only by 61 per cent and share in world exports fell to 20.7 per cent.

On the side of imports also we find slower growth and a declining share. It is clear that sluggish export expansion has affected import capacity.

Table 2.3 points to a fact of greater significance. By 1961 imports had expanded to the extent of 65 per cent over the level of 1948 while exports had expanded only to the extent of 61 per cent.

The deficit which thus arose has widened and assumed complex features with the passage of time. The developing countries thus face payment problems just when their import requirements are increasing fast.

Economic aid in the form of loans and grants helped the developing nations to some extent but not to the extent needed. Aid has unfortunately got entangled in politics and it is increasingly realised that aid could be no substitute for trade. That faith should not be placed on aid was proved during the recent conflict between India and Pakistan. The only remedy for the situation is to turn "under-developed countries need aid by means of trade" Ignacy Sachs. Aid or Trade. A.I.C.C. Economic Review. Republic Day Special Number. 1963.
push up exports so that larger supplies of foreign exchange could be obtained for purposes of development. How this could be achieved in the face of declining demand for their export and their own incapacity to increase exports in various lines so that their pace of economic development is not slowed down is the dilemma confronting developing countries.

III.

PRICES OF EXPORTS AND IMPORTS

The sagging demand for the exports of the developing countries is further reflected in their incapacity to control the prices of their export products. International markets being highly competitive the developing countries have little chance of influencing the prices of their products. High prices for import products also stimulate attempts at internal production. The successful expansion of raw jute production in India in the years following partition is an instance in point. The production of substitutes, both natural and synthetic, is another possibility. The result of these circumstances is that the developing countries have little bargaining power.

The developing countries are in a position of disadvantage also with regard to the prices of their imports. The problem arises because there are not many countries which are in a position to supply the capital goods required by the developing countries. A choice has, therefore, to be made from among a few countries. Foreign exchange difficulties further restrict the range of choice. The result is that the developed countries are able to charge higher prices for their exports in spite of the fact that their costs of production are lower.
due to higher labour productivity. On the other hand the developed countries benefit from technical improvements in primary production in the developing countries.

The developing countries thus find that the prices of their exports have either been falling or have not improved appreciably over the past few years while the prices of their imports are steadily rising. This also shows that the intensity of demand of the developing countries for the exports of the developed countries is greater than the intensity of demand of the later for the exports of the former. The developed nations have succeeded in maintaining their superior economic position by attaining a high level of technical efficiency and by diversifying their industrial systems so as to capture wide markets. The developing nations, on the other hand, are still far behind in these respects. Their export trade is still based on the nineteenth century pattern, but the character of their imports has definitely changed during recent years.

Between 1952-‘54 and 1962-‘63 the export unit values showed a small rise in the case of developed countries, but fell by about 10 per cent in the case of under-developed countries.31. The terms of trade of the latter fell by 9 per cent during the same period as shown in Table 2.5. It has been calculated that this meant a loss of about $2.5 billion on the export trade of the underdeveloped countries as a whole.32. Thus in the decade ending 1963 the modest growth in the volume of exports was to a great extent wiped off by a fall in export prices. In short the developed countries have been greater

### Table 2.5

**INDICES OF TERMS OF TRADE**

*Base 1958 = 100.*

<table>
<thead>
<tr>
<th>Year</th>
<th>Developed Areas</th>
<th>Developing Areas</th>
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<tbody>
<tr>
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</tr>
<tr>
<td>1952</td>
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<td>97</td>
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<td>1957</td>
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<td>99</td>
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<td>1961</td>
<td>104</td>
<td>97</td>
</tr>
<tr>
<td>1962</td>
<td>105</td>
<td>95</td>
</tr>
</tbody>
</table>


Beneficiaries of international trade and future trends also seem to be in their favor. In the words of one writer: "... international trade is a malnutritious 'meal' for the under-developed areas and the nutrition is sapped by the developed areas to make their 'dessert' more dainty." 33.

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33. P. Kumar. *Pattern of International Trade During 1951-62*. Eastern Economist. Vol.47, No.10. September 2, 1966. The quotation has reference to the statement of Walter Kruse (The International Economy. Page 30) that "the relationship of international trade to the American economy may, in a sense, be thought of in terms of a dessert after a meal, while for many economies international trade is more like the meal itself."
It is in the light of these facts that we have to consider the view that the prevalence of high prices for raw materials has stimulated the developed countries to evolve synthetic products and new processes of production. Thus according to Prof. A.K. Cairncross the failure of industrial countries to expand their imports of primary products between 1937 and 1957 in proportion to their economic growth was mainly due to higher prices. In other words he stressed the existence of low elasticity of supply and pointed out that in post-war years the governments of primary-producing countries were "more concerned to skim" off finance for other forms of development than to let high prices do the job of increasing production for such primary export commodities. The C.A.T.T. report for 1956 also supported this argument by pointing out that schemes of industrialisation pursued by the under-developed countries were responsible for the lag in exports. This approach, however, has not secured general support. Nurske himself regarded supply factors as arising from reactions to unfavourable demand conditions in the export market. A study of raw material prices during the first half of the present century shows that, in general, the producers have not benefited much as a period of rising prices has almost invariably been followed by a period of falling prices and the two have just cancelled the effects of each other. The period referred to by Cairncross was also abnormal due to the second world war and

35. Ibid.
Korean war. Thus the trend of development fits more closely with the demand deficiency argument.\textsuperscript{37}

IV.

FOREIGN TRADE POLICY

The problem facing the developing countries is thus one of rapidly mounting imports and sagging exports. It has been pointed out that their imports should grow at the rate of 6 per cent per annum if the U.N. development decade target of 5 per cent economic growth per annum is to be attained. That this target of growth is itself by no means ambitious is evident from the fact that population in the developing countries grows generally at the rate of over 2 per cent per annum. There is thus a case for more rapid growth.

But this depends on import capacity which comprises export earnings, invisible earnings and external assistance. While export earnings have been stagnant, invisible receipts have been just nominal and external assistance a mere trickle. In any case external assistance can only be a temporary push to the economy. The ultimate solution still lies in an increase in exports and commercial policy should be directed towards achieving this aim.

The basic need is to break the stagnant nature of the productive systems of the under-developed countries. The fact is that technical improvements, the development of synthetics and such other factors which have affected the demand for the exports of the under-developed countries are the inevitable results of economic

growth and have to be accepted as such. To put it briefly it is backward technique which holds back progress in under-developed countries. It, therefore, follows that there should be structural economic changes leading to a change in the pattern of trade so that the two fit into changed world conditions.

DIVERSIFICATION OF PRODUCTION AND EXPORT:

Under-development, by definition, points to the under-utilization of available resources and economic development comprises the systematic utilization of resources. The diversification of exports, the absence of which is largely responsible for the foreign trade difficulties of the under-developed countries, can be achieved only through the diversification of production which is just another name for economic development. We have thus a situation wherein economic development is possible only through larger imports earned mainly through larger exports which, in turn, have to result from economic development. This position of "circular and cumulative causation" is now tackled in most under-developed countries through economic planning leading to the diversification of production and export.

As economic development is a long-term process and imports are immediately required it will be a desirable first step to secure the maximum benefit out of the existing export structure. Attempts should be made to find outlets for existing exports in larger quantities and in areas which have not been tapped so far. Markets should

be found also for other natural products which may be available. These commodities have a low capital co-efficient and their supply can be increased with small investments. But serious efforts should be made to find new markets rather than stick to traditional ones. These imply a thorough study of agricultural and mineral possibilities in the country concerned and the modernisation of processes of production in stages. The resources required for these improvements should be mobilised mainly from domestic sources. In the final analysis this is a suggestion for agricultural reconstruction. An agricultural revolution has in fact preceded or accompanied industrial changes in all developed countries. Agricultural development should, therefore, be regarded as of basic importance from the point of view of trade policy.

The processing of crude materials before export will be another step in the diversification of export. In fact labour-intensive production should be utilised to the fullest extent to push up exports. The manufacture of consumer goods based on locally available materials such as textiles, shoes, household articles also lead to export prospects. The possibilities of developing light engineering and electronic goods should also be explored as these goods have low capital-output ratios.

Regarding the production of capital goods in under-developed countries it is sometimes argued that it should wait till some progress is made in economic development. This argument is defective. Firstly the developing countries find it difficult to secure capital goods from the developed countries due to lack of purchasing power. Secondly the developed countries have started
expanding primary production and also export primary products. Technological superiority is the factor behind this development. Under such a situation the under-developed countries cannot minimise the importance of basic industries. In the case of small countries such basic industries may be developed on a regional basis while the bigger countries should go ahead with the development of basic industries in a planned manner. Actually it is in this sphere that foreign aid assumes importance.

RESTRAINTS ON CONSUMPTION: In the industrial countries production grows fast mainly because they have well-developed internal markets. In the under-developed countries, on the other hand, the production of several goods cannot be taken up because of small domestic markets. From this point of view there is a case for developing internal markets. But in developing countries the domestic market can only be regarded as a base from where exports might take off. There is a real dilemma in this situation. It can be resolved by steadily increasing exports.

The importance of restraining consumption so that savings may be converted into investments leading to larger exports and greater capacity to import cannot be exaggerated. Restricted consumption and savings played an important part in the economic development of western countries. These countries were fortunate as wage-levels were low during their period of development and it was possible to re-invest their profits on a large scale. In fact there was no difference between this method and the more direct method of keeping consumption low adopted later by the U.S.S.R. Japan did not have to face this problem as the traditionally low
consumption prevailed till recently. The developing countries of the present, however, face a situation resulting from the operation of the 'demonstration effect'. They should, therefore, introduce suitable fiscal devices in order to restrain consumption.

**IMPORT SUBSTITUTION:** While the diversification of export constitutes one side of the medal the other is import substitution. Import substitution has been defined as "an increase in the proportion of goods that is supplied from domestic sources and not necessarily as a reduction in the ratio of imports to total income". It helps conserve foreign exchange and creates additional export capacity. Tariff protection for import substitute industries is also accepted as legitimate.

It cannot, however, be taken for granted that import substitution will lead to a saving in foreign exchange. The initial effect is often an increase in imports of various materials required for industry. This points to the need for maintaining exports at the highest possible level. In short, import substitution should not be pursued in isolation but should be integrated with schemes of export promotion.

41. "Industrial costs higher than import prices do not necessarily mean that an industry is not economic for a country as is sometimes assumed. Of course the smaller the difference the better .... It is not really a question of comparing industrial costs with import prices but of comparing the increment of income obtained in the expansion of industry with that which could have been obtained in export activities had the same productive resources been employed there". R. Prebisch. Ibid.  
As late-comers in the field of industry the under-developed countries will face a formidable problem in pushing up their industrial exports. But a few countries have already demonstrated the possibility of successfully exporting manufactures to developed countries. At present manufactures form a small but growing part of the exports of developing countries. In fact the rate of growth in the exports of manufactures from these countries is higher than that of any other major commodity group. Thus during the period 1955-1960 the total exports of the ECAFE region rose by 11.5 per cent, while the exports of manufactures rose by 40 per cent. The increase in export of manufactures to the developed areas was higher, namely 74 per cent.43. This shows that there is room for such exports. In fact it is possible that a realignment of production and export will be effected on a world-wide basis as the existing pattern of specialisation is not in all cases based on comparative advantage.44.

POLICY OF DEVELOPED COUNTRIES: It has also become necessary for the developing countries to take account of the trade policies followed by the developed countries. These policies have undergone fundamental changes in recent years. The complementary economic relationship between industrial countries and primary-producing countries has been affected by various developments and, as pointed out in Section II, the industrial countries now aim at self-sufficiency in primary goods.

44. "Perhaps in the near future the pattern of trade between developed and developing countries will rapidly shift from an exchange of primary goods for manufactured goods to an exchange of innovation-oriented for imitation-oriented manufactured goods (including less complicated capital goods in smaller units)". Shih-Chin-Yang. Op. cit.
with the help of protection. Groups of countries have been formed with protectionist aims. The result is that world trade is largely confined to the developed countries. In fact the U.S.A., the U.K. and the EEC countries together control 90 per cent of world trade. This imbalance in world trade is responsible for many of the difficulties of the developing countries.

A basic difference between the system of world trade which existed in the nineteenth century and that which exists today is to be noted. In the nineteenth century Britain followed a free trade policy and her imports from the colonies and other dependences increased as steadily as her exports. The under-developed countries thus benefited to some extent. But in the post-second world war period the world economy is dominated by the U.S.A. which is almost completely self-sufficient in resources and follows a protectionist policy. There is no room for thinking that the U.S.A. would adopt a liberal policy in trade matters. In this connection Rangnekar quotes the example of the textile agreement of 1962 which was utilised by the U.S.A. to discriminate against textiles from Asia on the ground that they were low-wage exports and created "market disruption" in her territory.

The same protectionist attitude has been adopted by other developed countries too. The principle of reciprocal concessions has been invoked by them. This, however, is the wrong approach as it will stand in the way of the economic development of the under-

46. Ibid. Pages 94 - 95.
developed countries. Further, the developed nations themselves stand to benefit by adopting a liberal approach towards the developing nations. As Prebisch points out: "The reduction or elimination of such protection at the centres has an implicit element of reciprocity, since the resultant increase in exports of primary commodities from the periphery will be followed by a corresponding increase in its imports of industrial goods, in response to their high income elasticity of demand, and there is no need for any reduction or elimination of duties to obtain this result." But it is a short-sighted approach which now prevails.

The European Economic Community is a development of more serious consequence to the developing nations. According to Rangnekar, "the movement bears traces of frustration, and a lingering nostalgia for the vanished past". Britain is a candidate for membership in this body while the U.S.A. has shown interest in associating with it. If this development takes place a club of the rich nations of the world will come into existence. The E.E.C. has agreed to accept under-developed countries of Asia and Africa as associates. This reveals the mental make-up of the colonial powers and the divergence of interests between the two sets of nations was clearly brought out in the U.N. conference on Trade and Development held in 1964. The conference evolved a "chapeau" of measures for the diversification of world trade and suggested that each developed country should contribute 1 per cent of its national income as assistance to developing countries. These suggestions

47. Ibid.
48. Ibid.
The question arises why the underdeveloped countries themselves should not form regional bodies of the type of the E.E.C. The prospects for any such body are far from bright as these countries produce identical products and all are dependent on developed countries. Yet there is scope for economic cooperation among them. A really effective economic union among them appears to be impracticable not only for economic reasons but also due to political rivalries and jealousies.

The conclusion which emerges is that the underdeveloped countries should concentrate their energies on economic development. In this they stand to gain by emulating the example of the U.S.S.R. without necessarily subscribing to the Russian ideology. In the late twenties and the early thirties the U.S.S.R. acquired capital goods from the U.K. and the U.S.A. by exporting agricultural products and raw materials. All attention was concentrated on exports during this period and consumption was strictly controlled. The prices of exports were adjusted according to the requirements of the situation. All this was possible because the state exercised effective control over these matters. There is a strong case for some such system in the developing countries. In short exports should be promoted at any cost in order to acquire capital goods for basic industries. Import substitution should be resorted to in order to produce everything possible and economical within the country. Consumption should be controlled through fiscal and other measures. The state should play an active part in regulating foreign trade in the national interest. These may be regarded as the main lines on which foreign trade policy should be formulated in the developing countries.