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The consequences of economic change in the developing countries
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To talk about developing countries in today's world implies making
generalisations which cannot always be justified. If, in the last cen­
tury, or even in the middle of the last century, it was relatively easy
to classify nations in terms of their respective levels of economic de­
velopment, such practice is made much more difficult nowadays by
virtue of the enormous variations to be noted in those criteria which
are usually accepted as indicators of economic progress.

In 1985 the two most heavily populated nations of the world, China
and India, had an annual per capita income of US$ 290; in Ethiopia,
this income was no more than US$ 110. In an intermediate posi­
tion were to be found countries such as Peru (US$ 1285), Colombia
(US$ 1320) and Syria (US$ 1560). After these countries, with a
slightly higher level of income, came Brazil (US$ 1640), Malaysia
(US$ 1288), Portugal (US$ 1970), Venezuela (US$ 3080) and Greece
(US$ 3550). Finally, at the top of the pyramid were to be found Is­
rael (US$ 4990), Hong Kong (US$ 6230) and Singapore (US$ 7420),
with the high income petroleum exporting countries being excluded
from this list.

The great disparity in terms of these countries' per capita income,
which reaches a ratio as high as 70 to 1 (Singapore and Ethiopia), is
even more notable than the ratio between the GDP of middle income
developing countries (approximately US$ 1300) and the average
GDP of the free market industrialised economies — US$ 11,810.
Even if we take into account the particular case of the USA, where
per capita income in 1985 amounted to US$ 16,690, the ration of
this latter country's income is not even as high as 13 to 1.

Such discrepancies are even more serious when the indicators for
the distribution of income are taken into account. The inequalities in
per capita income are reflected in truly brutal differences in the wel­
fare of the different populations, especially when one considers that
the percentage share of the richest 10% of the population in the in­
come per household of developing countries is in all cases higher
than 30%, whereas the percentage share of the poorest 20% is no more than 7% of that income, in those countries for which statistics are available. In fact, the income of the richest 20% of the population is frequently 6 or 7 times greater than that of the poorest 20%; in Brazil and the Ivory Coast, this indicator of inequality reaches such extremes whereby the ratio is close to 30 to 1 (33:1 and 25:1, respectively). By way of comparison, and according to the figures provided by the World Bank, the highest such ratio noted in the free market industrialized economies was one of 8.7% in Australia and New Zealand. In the USA, this ratio was 7.5%; in Sweden, it was 5.6%; and in Japan and Holland 4.3%.

These discrepancies in incomes, further exacerbated by the inequalities evident in their distribution, equally give rise to enormous variations in social indicators. At the lowest level of developing countries, average life expectancy is approximately 50 years of age (Bhutan 44 years, Ethiopia 45, Pakistan and Bangladesh 51), whereas, at the uppermost level, average life expectancy in several countries is more than 70 years of age, a figure which is very close to the average of the free market industrialized economies (76 years), as is shown by the following statistics: Brazil 65 years, Mexico 67, Argentina 70, Uruguay 72 and Portugal 74.

In the poorest countries, the number of students enrolled in secondary education amounts to an average of 32% of the appropriate age group (Ethiopia 12%, Burma 24%, India 34% and Zaire 57%; in the middle income developing countries, this figure reaches an average of 56% (Brazil 35%, Portugal 47%, Mexico 55% and Greece 82%). For the free market industrialised economies, the figure is 90%. Per capita energy consumption, measured in kilograms of coal per year, is 692 kg in Equador and 3,029 kg in Venezuela. Only 50% of people living in Mexico have running water in their homes, whereas in Uruguay the corresponding figure is 81%.

In short, the inequalities are so great that it becomes difficult to adopt a uniform approach to the problem of growth and economic development. At the same time, one is faced with problems of geographical and cultural differences and the differing historical evolution of each society. How can one make a genuine comparative analysis between Latin America, where in 1960 several countries
had a per capita income that was higher than those of Japan and a number of European countries, and African countries which have never managed to overcome the most abject poverty? In the first decades of this century, Argentina had a per capita income that was equivalent to that of France. Today this income is lower than those of Spain and Greece and equivalent to that of Korea.

In 1960, per capita income in Uruguay and Venezuela was higher than in Italy, Spain and Japan; in Argentina, it was three times higher than in Korea, and in Chile it was very close to that of Spain and higher than in Portugal and Greece. However, by 1985, the highest per capita incomes in Latin America were no greater than US$ 2,800, whereas per capita income in Korea had risen to US$ 2,648, in Japan to US$ 7,130, in Italy to US$ 4,808, in Spain to US$ 4,336, in Singapore to US$ 5,000 and in Formosa to US$ 3,160.

At the same time serious discontinuities have been noted in the economic evolution of developing countries. The evident tendency towards economic stagnation in several countries, as is the case for example in certain African nations, in Asia and in Latin America, contrasts very sharply with the meteoric explosion in terms of economic growth noted in Japan and other Asian countries such as Singapore, Korea, Taiwan and Hong Kong. In the middle of these two extremes, one finds the cases of the Latin American economies, which showed signs of a certain dynamism until the end of the 1960s, but then, with the possible and still rather uncertain exception of Brazil, have spent the last twenty years confronted with an economic stagnation that threatens to become chronic and consequently more and more difficult to overcome.

In the face of such diversities, how should one begin to point out the necessary path to economic development?

What is expected from the developed countries

With the exception of the Soviet Union and certain other socialist countries, the GDP of the developed economies is equivalent to approximately four times the total value of the GDP of the developing countries — roughly US$ 2,500 billion as against US$ 10,000 bil-
lion. Playing, as they do, such an important role in the generation of goods and services worldwide, the economic policies adopted by the industrialized countries have now become an essential factor in determining the evolution and progress of the poor countries.

In its most direct form, the inter-relation between development and underdevelopment occurs by means of two major channels — international trade and external savings. In as much as the evolution of these two elements depends on the evolution of the economic growth of rich countries, the economic development of poor countries is also inextricably bound up with the performance of the major economies of Europe, Japan and the USA. Consequently, the continued economic growth of the high income industrialized economies is a necessary condition for any effort being made towards an intensification of economic growth in the developing countries.

Between 1965 and 1973, the average annual growth rate of the free market industrialized countries was 4.7% per year; between 1973 and 1980 this rate fell to 2.8%. In 1984, there was a growth rate of 4.6%, but immediately afterwards it returned once more to the general pattern of the last fifteen years, being 2.8% in 1985 and 2.5% in 1986. During this same period, the average annual growth rate of Third World countries fell from 6.5% between 1965 and 1973 to 5.4% between 1973 and 1980. In keeping with the pattern noted in the richer economies, average growth in 1984 reached a level of 5.1%, thereafter falling in 1985 and 1986 to 4.8% and 4.2% respectively.

There is therefore a powerful correlation to be noted between the two trends in growth rates, which is clear evidence of the existing connections between the rich and the poor countries of the world.

The first link between the two is that of international trade. Approximately two thirds of exports from developing countries go to the industrialized economies, whereas roughly 70% of the exports from rich countries are distributed amongst these countries themselves. The asymmetry of this situation is glaringly obvious. The developing countries depend essentially on imports from the industrialized countries, whereas only 25% of the latter’s exports are destined for the former. (See Table 1).

Since the middle of the 1970s, there has been an enormous regression in the world trend towards the liberalisation of international
trade, which first started after the Second World War. International agreements on tariff reductions did not spread to agricultural produce and industrial goods exported by developing countries to the same extent as they did to exports from industrialized countries. And the world recession of 1974-1975 led to a new wave of protectionism in the industrialized countries, which thus implied the use of new instruments such as price controls, quality controls, «voluntary» limitations and other types of restrictions.

The important thing that should be stressed, however, is that this neo-protectionist movement most seriously affected the developing countries, and Latin America in particular. In 1984, almost 21% of the industrialized countries’ imports from Third World countries were subject to non-tariff restrictions, as opposed to 11.3% of the products of the rich countries.

If the economic growth of the poor countries is to be sustained, there are some basic requirements that need to be met:

a) an average growth rate of at least 3% per year in the industrialized economies;

b) a greater opening up of the markets of the industrialized countries to goods from the developing countries, principally though a reduction in protectionism, whether veiled or explicit;

c) a greater stability in the exchange rates of the currencies of the developed countries.

It is generally agreed that, if these objectives — important not only for the stability of the developed countries, but also for stimulating the economic growth of the poor countries — are to be reached, the USA needs to establish a fresh equilibrium between its fiscal and monetary policies, by reducing the level of its internal demand and consequently its budget and trade deficits. At the same time, it is the task of the more dynamic countries, such as Germany and Japan, to expand their economies in such a way as to help maintain the objective of a minimum average growth rate of 3% per year for the rich nations as a whole.

The 1987 crash of the world’s principal stock markets served as a first warning for the urgent necessity for the USA to take corrective measures. Most likely, the conditions do not exist for the fall in
the stock market to become transformed into a worldwide depression. The speedy reaction of the North American government in rapidly expanding the liquidity of its economy — and thus avoiding repeating the mistakes made in 1929, when there was a movement in the opposite direction which served only to deepen the recession — may help to avoid an even greater slump in the world economy. At the same time, however, this policy option will probably bring about a run on the dollar, with all the disadvantages that this entails.

TABLE 1:
ORIGIN AND DESTINATION OF EXPORTED GOODS
(as percentage of total at origin)

<table>
<thead>
<tr>
<th>Origin</th>
<th>Free Market Industrialized Economies</th>
<th>High Income Petroleum-exporting Countries</th>
<th>Developing Countries</th>
<th>Others</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low income</td>
<td>—</td>
<td>52</td>
<td>—</td>
<td>4</td>
</tr>
<tr>
<td>Lower middle income</td>
<td>74</td>
<td>71</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>Higher middle income</td>
<td>64</td>
<td>62</td>
<td>(.)</td>
<td>2</td>
</tr>
<tr>
<td>High-Income Petroleum-exporting countries</td>
<td>70</td>
<td>59</td>
<td>3</td>
<td>1</td>
</tr>
<tr>
<td>Developing countries</td>
<td>67</td>
<td>63</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>Exporters of manufactured goods</td>
<td>52</td>
<td>53</td>
<td>1</td>
<td>3</td>
</tr>
<tr>
<td>Countries heavily in debt</td>
<td>74</td>
<td>71</td>
<td>(.)</td>
<td>1</td>
</tr>
<tr>
<td>Free market industrialized economies</td>
<td>70</td>
<td>71</td>
<td>1</td>
<td>3</td>
</tr>
</tbody>
</table>

Source: World Bank
TABLE 2: SAVINGS AND INVESTMENT
(% of GNP) - 1965/1985

<table>
<thead>
<tr>
<th>Country</th>
<th>Investment/GNP</th>
<th>Gross National Savings/GNP</th>
<th>Gross External Savings/GNP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argentina</td>
<td>19.8 21.8 16.3</td>
<td>19.7 21.2 11.3</td>
<td>0 0.6 5.0</td>
</tr>
<tr>
<td>Brazil</td>
<td>26.1 26.2 20.4</td>
<td>24.3 21.7 16.9</td>
<td>1.7 4.5 3.5</td>
</tr>
<tr>
<td>Mexico</td>
<td>21.4 25.2 25.4</td>
<td>19.9 21.3 23.5</td>
<td>1.5 3.9 1.9</td>
</tr>
<tr>
<td>Venezuela</td>
<td>29.3 32.6 19.9</td>
<td>30.0 34.5 24.9</td>
<td>-0.7 -1.9 -5.0</td>
</tr>
<tr>
<td>Guatemala</td>
<td>13.3 18.7 13.5</td>
<td>12.9 16.4 9.9</td>
<td>0.4 2.3 3.6</td>
</tr>
<tr>
<td>Nigeria</td>
<td>21.0 26.5 18.7</td>
<td>19.4 28.3 16.4</td>
<td>1.7 -1.8 2.3</td>
</tr>
<tr>
<td>Zaire</td>
<td>13.7 15.0 14.6</td>
<td>9.8 8.8 7.2</td>
<td>3.9 6.2 7.4</td>
</tr>
<tr>
<td>India</td>
<td>18.4 22.6 24.4</td>
<td>17.9 22.3 22.6</td>
<td>0.5 0.3 1.8</td>
</tr>
<tr>
<td>Korea</td>
<td>25.1 31.8 30.7</td>
<td>21.5 26.4 26.9</td>
<td>3.6 5.3 3.8</td>
</tr>
<tr>
<td>Philippines</td>
<td>20.6 29.1 25.8</td>
<td>20.6 24.3 20.0</td>
<td>0 4.8 5.9</td>
</tr>
<tr>
<td>Algeria</td>
<td>32.1 44.5 38.2</td>
<td>29.9 38.9 38.6</td>
<td>2.2 5.6 -0.4</td>
</tr>
<tr>
<td>Yugoslavia</td>
<td>29.9 35.6 38.5</td>
<td>30.0 32.9 37.9</td>
<td>-0.1 2.7 0.6</td>
</tr>
</tbody>
</table>

Source: World Bank

Differences in the patterns of growth

There is, however, one historical fact relating to international trade which immediately calls our attention: the contrast between those developing countries whose activity is geared towards foreign markets — the exporters of manufactured goods — and that group of countries which are heavily in debt. The former countries have more diversification in their exports, with only half of them directed at the developed countries. Those countries which are in serious debt, however, have more than 70% of their exports concentrated in those same markets. On account of the interest repayments that they are forced to make, this group of countries is obliged to generate large trade surpluses in strong currencies and consequently finds itself much more dependent on the markets of the developed countries.

But the question of foreign debts has its greatest impact on the growth potential of the Third World economies.
Those developing countries which are exporters of manufactured goods maintained an average growth rate of 7.4% between 1965 and 1973 and one of 6% between 1973 and 1980 (in contrast to the average growth rates for the developing countries as a whole of 6.5% and 5.4% respectively). Those countries which are in serious debt managed to achieve growth rates of 6.9% and 5.4% respectively, in other words ones which were very close to the overall average for the poor countries. As from 1982, however, with the crisis in international liquidity, the major exporting countries sustained an average growth rate of 6.3% until 1986, as against 0.75% for the countries with serious foreign debts.

There is no doubt that the external adjustments that were imposed on the countries in serious debt were brutal. The 1980s have already been called the «lost decade» in terms of economic growth, and, for those countries and their populations which are beset by poverty (in some cases by misery and starvation), the loss of an entire decade may well lead to frustration and revolt, with unforeseeable social and political consequences.

It is totally unnecessary to go into great detail about the foreign debt crisis. It will be enough to say that, between 1970 and 1985, the percentage of the Gross National Product of developing countries spent on servicing the State’s foreign debt increased from 1.5% to 4.3%. In the specific case of those countries most heavily in debt, the figures are 1.6% and 5.1% respectively; whereas, in those countries which are exporters of manufactured goods, the respective amount increased from 1.2% to only 2.7%. Certainly the situation is even more distressing if one also includes private debts.

The impact of the foreign debt crisis has forced those countries in debt to make a sharp cutback in their investment programmes. Without the possibility of fresh inputs of foreign resources ever since the beginning of the decade, these countries have been suddenly transformed into net exporters of capital, with its obviously harmful repercussions on the supply of savings and thus on the rates of capital formation and economic growth.

For most developing countries, the data available since 1985 show that there have been notable drops in investment and external sa-
vings (see Table 2). This trend is certainly getting worse. It is therefore of the utmost necessity that the rich countries make a genuine effort to prevent real foreign interest rates from reaching levels higher than the historic ceiling of 3%. Furthermore, if the alarming stranglehold that foreign countries have over most developing economies is to be overcome, then it is urgent that the flows of loan and risk capital, which underwent a sudden paralysis during the 80s, should be given fresh impetus.

Without the commitment of the industrialized economies to maintaining an adequate growth rate, a firm policy of opposition to the spread of protectionism, and, more than anything else, coordinated fiscal and monetary measures capable of reducing interest rates and stabilising exchange rates, it will be extremely difficult for the developing countries to reach even the minimum conditions necessary for embarking on a new process of growth. In its turn, the foreign debt crisis will continue to haunt the international financial community, rendering unviable those mechanisms used for the financing of the economic growth of the developing countries.

Growth options

One of the important things to be discovered is whether all the evils and contradictions which beset the underdeveloped countries are in fact originated by the behaviour of the industrialized nations. Is underdevelopment the necessary counterpart of the development of the industrialized countries? It is true that the developing economies are victims of an economic system which is by its very nature perverse?

To accept such a view of history would be tantamount to indulging in a most inappropriate form of determinism, and it would, at the same time, exempt the elites of the poor countries from any share of blame for their incompetence and lack of foresight, accusations which cannot easily be disregarded. In fact, an analysis of the growth patterns of certain groups of poor countries clearly shows that the models adopted are quite distinct and reflect deliberate choices and options in the determination of their economic policies.
The model for development adopted by those countries in the Pacific area which are exporters of manufactured goods has become a new paradigm for growth; it is like a new orthodoxy which has arisen in answer to the old recipes of CEPAL\(^1\) which had such an influence on economic planners in the first post-war decades.

The old orthodoxy proclaimed the need for import substitution at all costs, and industrialization was taken as being a renewed hope for prosperity. For these goals to be obtained, it was justifiable for the economies to be geared towards their own markets and for the new productive sectors to benefit from trade barriers which could protect them against foreign competition. At the same time, given the limited financial and management resources of a bourgeoisie that was only just beginning to emerge, ideal conditions were created for the emergence of a strong State capable of introducing into these economies manufacturing activities which were considered to be modern, while furthermore carrying out the heavy investments in infrastructures needed to support the new process of industrialization. In this inward-looking model, the State was to play the role of the major economic agent, by simultaneously performing the functions of producer, supplier and regulator of the economy.

\(^1\) CEPAL = Comisión Económica para América Latina. This is also referred to in English as ECLAC = Economic Commission for Latin America and the Caribbean.

It should be pointed out that, by the middle of this century, economists had already begun to understand that the evolution of modern capitalism would be different from that suggested by the classical concepts. The structure and relationships of power and dependence between the rich countries on the one hand and the underdeveloped countries on the other called for government action to try and prevent a disequilibrium of forces that threatened to perpetuate a disadvantageous international division of labour. The production and distribution of goods took place within the framework of a market structure characterised by evidence of a certain concentration, thus making government participation an essential factor in the defence of national interests.

Against the background of this view of economic matters, several countries, mainly Latin American ones, unleashed a vigorous pro-
cess of economic growth. As we have seen, this movement showed signs of being capable of bringing the values of the per capita income of certain Latin American countries closer to those exhibited by the developed economies of Europe. It seemed as though the formula for worldwide economic progress had finally been found.

Initially, it was seen as the job of the State to generate the appropriate means for the financing of this effort towards industrialization, either by means of internal savings or through the management of income transfers from those sectors which had available savings to those which were badly lacking in resources. In its second phase, the process was continued on the basis of loans granted by the commercial banks, which were eager to recycle their petrodollars.

This model of development enabled the most important Latin American countries to attain a reasonable level of industrialization during the 1950s. After the substitution of imported consumer goods, a more arduous process of industrialization was started in the areas of intermediate goods and consumer durables, and more recently in the fields of capital goods and basic consumer goods.

The increasing and quite natural difficulties required these countries to adopt an increasingly more closed and concentrated model, if they were to obtain economies of scale, and an increasingly more State-run economy. As a result, these economies have emerged in the 1980s showing signs of great fragility in regard to their possibilities of international competition. The heavy protection that they have been given has given rise to inefficient industrial sectors which are heavily subsidised and very poor in terms of technology. In essence, they lack the necessary confrontation with the market.

With the foreign debt crisis, which made its sudden and violent appearance on the scene in 1982, these economies found themselves obliged to make sharp adjustments if they were to continue to be able to service their foreign debts. And these countries, which followed the recommendations of CEPAL, find themselves today confronted with deep economic recessions.
In sharp contrast to this growth model, a new orthodoxy appeared at the beginning of the 1970s, based on the experience of the «Asian tigers».

The opening up of the economy to foreign markets, respect for the rules of the free market, and the fundamental emphasis on private enterprise, are the mainstays of this new model of development, whose success has been proved by the economies of countries such as Japan, Singapore, Hong Kong, Taiwan and Korea. As we have already seen, these countries have, in the last few decades, shown substantially higher growth rates than those of the Latin American economies, and they have managed quite rapidly to outmatch the per capita GDPs of those countries which chose to follow the alternative path of giving preference to the domestic market.

The Asian countries succeeded in obtaining international finance, but the recent liquidity crisis has not affected them anywhere near as much as it has the other regions of the world. Even during periods of crisis, these countries have continued to invest in export-oriented sectors. They have thus managed to generate sufficient earnings in foreign currency to be able to meet their foreign commitments without needing to make any greater internal adjustments.

Is should be remembered that certain countries, notably Brazil, adopted strategies that were a mixture of the import substitution model and the export-oriented one. However, attempts to liberalize the economy did not have the same continuity or consistency as did the Asian economies.

How can we assess these two different routes towards economic growth? Are they conflicting ones? Is the choice a bi-reciprocal one? Let us take as an example the following economic policy (as highlighted by the economist Jeffrey Sachs): a country pegged its currency to the dollar in 1950 and maintained a fixed nominal parity, in absolute terms, for more than 20 years. For the first 15 years of that period (until 1964), the exchange rate was strictly controlled by a government agency and the currency was always overvalued, by about 60% in the 20 year period. A law relating to the control of
trade and the exchange rate dating back to 1949 gave the government a monopoly of the purchase of foreign currency and made it the only lawful source of such currency. Unwritten laws governed its distribution. Bureaucrats allocated this money to the more favoured sectors, giving most attention to private companies, in whose growth they had a special interest. The internal capital market was highly controlled and completely isolated from the international markets. Direct foreign investment was severely limited and majority shareholdings by foreign companies were banned both legally and administratively. From the beginning to the middle of the 1960s, approximately one third of external funds for industrial investment originated from loans from government financial institutions, at subsidised rates of interest. These government institutions continued to be an important source of cheap finance until the end of the 1960s. Would anyone care to hazard a guess as to the name of this country? It is in fact Japan.

Consider further the high level of Japanese state intervention in the question of the organization of foreign trade and of the support given to export-oriented sectors; consider also the efforts made by the Koreans in creating their enormous trading companies; consider the importance of the state sector in Taiwan and Korea, which is equivalent to 35% and 25% respectively of those countries’ gross capital formation; consider the role played by the Korean government in setting up that country’s iron, steel, chemical and other industries; consider the transfers of US dollars which financed a large part of Taiwan’s and Korea’s imports between 1955 and 1959.

In fact, if we consider all these factors, it will be noticed that the liberalizing / export-oriented model followed by the Asian countries is very similar to the import substitution model adopted by the Latin American countries, with a major role being played by an interventionist State. This model has nothing to do with the one of free competition and economic liberalism that people are trying to associate nowadays to the growth model of the Asian exporters.

There are differences from the CEPAL model, as for example the fact that the economic policy of the Asian countries has been constantly oriented towards foreign markets, but the question of State
intervention was certainly not one of the most noticeable differences between the two growth models analysed here. It should further be recognised that the nature of this State intervention was different, since in the Far Eastern countries all economic policy measures always ended up being subjected to the test of the foreign market.

What lessons are to be drawn from this brief analysis of these two patterns of development?

It can be seen that the phase of import substitution, with greater emphasis being given to the domestic market and characterised by the indispensable intervention of the government, is a stage through which all the higher income developing countries passed, to a greater or lesser extent. In this way, one cannot deny the importance of both state intervention and the promotion of import substitution in those low income countries which still need to begin the process of structural transformation.

On the other hand, it must be admitted that, once this first stage had been completed, the Latin American countries then pursued a growth policy which soon found itself, and still finds itself, coming to an abrupt halt, while the economies of those Asian countries which are exporters of manufactured goods have shown the necessary flexibility and capacity for change, which have helped them to achieve remarkable rates of economic growth.

There is not, unfortunately, just one recipe for economic growth. Liberalisation, privatisation, and the orientation of the economy towards foreign markets, are urgent and indispensable steps that need to be taken by countries such as Brazil, Argentina, Mexico, Venezuela, Turkey, Greece and many other countries which have already reached a minimum level of industrialization. In these cases, competition and the diminishing importance of the State, thereby making room for private enterprise to lead a new wave of economic expansion, is the only way of escaping from the chronic stagnation afflicting those countries which refuse to evolve towards a new stage in the growth process.
However, for those countries which still find themselves beset by the problems of a state of profound underdevelopment, the interventionist model of import substitution is still the one which can offer them the best prospects for the future.