



THE UNITED STATES AND THIRD WORLD
POOR IN THE INTERNATIONAL ECONOMY:
SOME ECONOMIC AND ETHICAL ISSUES FOR
DISCUSSION

Ernest Bartell, c.s.c.

Working Paper #29 - December 1983

Father Ernest Bartell is the Executive Director of the Helen Kellogg Institute for International Studies and Professor of Economics at the University of Notre Dame. This paper was prepared for presentation to the members of the United States Catholic Bishops' committee preparing a pastoral letter on the American economy.

ABSTRACT

In mainstream economic models of free markets, optimization criteria take on a greater priority than other important value considerations. However, the most efficient allocation of resources in a competitive free market does not necessarily lead to a distribution of income and wealth which meets acceptable ethical standards of social justice and human equality.

Distribution of gains from international market activity tends to be biased against Third World countries, and particularly against the poor within those countries. An adequate economic and ethical evaluation of United States international economic policy must take this into account.

Value judgements about distribution, though they affect the domestic economic policy of most countries, historically have had little influence on the workings of international markets. The richest fifth of the world's population accounts for 50 times the per capita GNP of the poorest fifth and, in the absence of international intervention, the inequality will continue to grow because of the biases against the poor nations in markets for labor, goods and services, and financial capital.

This paper examines these distributional biases together with some policy options proposed to redress them, and concludes that only a broad based popular appeal grounded in the considerations of higher ethical and moral values, as well as in the requirements for survival of an international economic system, is likely to create the collective will necessary for a comprehensive and coordinated approach to a rational distribution of economic means and opportunities in an increasingly interdependent economic world.

RESUMEN

En los modelos económicos de libre mercado convencionales, los criterios de optimización adquieren una más alta prioridad que otras consideraciones valóricas de importancia. Sin embargo, la asignación de recursos más eficiente posible en un sistema competitivo de libre mercado no asegura una distribución del ingreso y riqueza que satisfaga las normas éticas de justicia social e igualdad entre los hombres.

La distribución de las ganancias que se crean como resultado de la existencia de los mercados internacionales tienden a discriminar en contra de los países del Tercer Mundo, y en particular en contra de los pobres al interior de dichos países. Una evaluación adecuada de la política económica internacional de los Estados Unidos, desde el punto de vista económico y ético, debe tomar en consideración los aspectos mencionados.

Los juicios de valor en relación con los resultados distributivos, si bien afectan a las políticas económicas domésticas de la mayor parte de los países han tenido, históricamente, poca influencia sobre el modo de operación de los mercados internacionales. Al veinte por ciento mas rico de la población mundial le corresponde un producto nacional por persona 50 veces superior al del 20% mas pobre y, en ausencia de intervención internacional, esta desigualdad continuará aumentando debido a la discriminación que existe en contra de las naciones pobres en los mercados del trabajo, de bienes y servicios y de capital financiero.

Este trabajo examina estos sesgos distributivos así como algunas opciones de políticas que se han propuesto para corregirlos y concluye que sólo una aceptación y acuerdo popular amplios, basados en altos valores éticos y morales, así como en los requisitos para la sobrevivencia del sistema económico internacional, pueden crear la voluntad colectiva requerida para un enfoque suficientemente amplio y coordinado con respecto a la distribución racional de recursos y oportunidades económicas en una economía mundial que es cada vez mas interdependiente.

THE UNITED STATES AND THIRD WORLD POOR
IN THE INTERNATIONAL ECONOMY:
SOME ECONOMIC AND ETHICAL ISSUES FOR DISCUSSION

Introduction

Despite the fact that value questions are invariably present, explicitly or implicitly, in economic decision-making, discourse between the fields of economics and of ethics seems inevitably difficult. Mainstream economists, armed with the analytic tools of positive economics, are conditioned to ignore, accept as given or assume away virtually all value judgments except those implicit in the normative criteria of efficiency and maximization. These are the criteria that determine "optimal" solutions in much of the analysis of resource allocation and economic growth, especially through the markets for final products and services and for factors of production like labor and capital. In the eyes of the ethicist the methodology of positive economics thus gives operational priority to one set of values, those related to efficiency and maximization, over other normative criteria, especially the human values affecting and affected by the distribution of income and wealth.

The circular flow of income that underlies positive economic analysis in fact acknowledges the interaction between the distribution of income and wealth and the behavior of an economy with

respect to resource allocation and economic growth. It recognizes the influence of markets and prices upon the determination of how the benefits of economic activity shall be distributed among the participants in the economy. It also recognizes the influence that the spending habits of those with varying shares of income have upon subsequent resource allocation and growth. The spending decisions of a single hypothetically wealthy economic participant who receives the lion's share of the income generated in an economy are likely to result in different employment opportunities and a different set of goods and services produced than the spending decisions of a population receiving more modest, relatively equal shares of income.

Most models of economic analysis, however, assume distribution to be socially given or held fixed through some hypothetical and instantaneous social mechanism for redistribution so that the analysis can isolate the operation of other normative criteria, e.g., efficiency and maximization, without concern for the interaction of distribution with those other criteria. Ethicists, on the other hand, come to economics from different premises, e.g., those based upon philosophical or theological perceptions about human equality, society and justice whose economic implications immediately relate to questions of distribution. So it is not surprising that those familiar with the importance of efficiency criteria in economic analysis, especially the analysis of markets, are apt to criticize the do-gooders for too much emphasis upon distribution in their evaluation of economic systems.

The efficiency norm has thus come to be a potent and popular weapon for apologists of free markets as the best hope for successful economic development in the Third World. [1]

However, it is also important for those who would understand the actual possibilities and constraints for development in the Third World to attend closely to the ways in which the gains from development are actually distributed, especially in the socially unregulated international marketplace. For a variety of historical and technical reasons the distribution of gains from market activity in international markets for products and services, for labor and for capital is frequently biased against the poor countries of the world and against the poor within those countries. Hence, for an adequate understanding of the possibilities of development in the Third World the questions of distribution cannot be assumed away as neatly as they are in conventional positive analysis.

Moreover, the questions of distribution that arise from the workings of international markets raise ethical issues for developed countries, especially the United States, whose economic policies can directly influence the markets for products, financial capital and labor upon which developing countries depend. The balance of this paper seeks to identify some of the analytical links between distribution and development in economics that have ethical implications in the context of Catholic social teaching. Special emphasis is given to the distributional biases against the poor of the Third World in international markets for

products and services, for labor and for financial capital with some attention to the role of United States economic policy and practice in shaping those markets.

Development and Distribution

The United States relates economically to the developing countries of the Third World with the same categories of two-way transactions that determine domestic and other international economic activity, e.g., the buying and selling of goods and services, financial transactions and flows of capital through direct investment, loans and grants across both private and public sectors. Nevertheless, the scope and intensity of ethical discussion about economic relationships between developed and developing countries (perhaps especially within developing countries) is frequently greater than that concerning economic activity within or among developed nations.

Most professional economic analysis in the United States explicitly excludes from consideration all normative criteria, with the exception of the criterion of efficiency or maximization in the allocation of the world's resources, which, like the instruments of economic activity, is morally ambiguous or neutral. There is no necessary inherent relationship, positive or negative, between efficiency in the marketplace or maximization of growth rates, for example, and ethical norms of social justice.

Economic development, however, is much more than efficient economic growth. Economic development is sometimes characterized

as growth with equity, where equity embraces implicit and explicit judgments about distributional inequality-- inequality in the distribution of the preconditions for growth and inequality in the distribution of the benefits of growth for both private and social purposes.

The normative criteria for distributive justice in Catholic social teaching are principally based on human values, namely, the possession of rights that are determined not in economic systems and economic analysis, but in the dignity and worth of all human persons as created in the image of God and united in the redemptive love of Jesus Christ.[2] It is these universally shared rights that ground ethical evaluation of both the freedoms and the inequalities generated by systems of economic production, exchange and growth. We appeal to these same rights to justify personal freedoms as well as the limitation of personal liberties by collective values embraced in such norms as the common good or human solidarity.

Also acknowledged in Catholic social teaching are distributional criteria based on principles of meritorious activity, such as, individual effort or personal contribution to social well-being.[3] But merit itself can be grounded on different ethical bases. Part of the ethical appeal of competitive free markets rests on the ability to demonstrate that such markets not only allocate resources efficiently in meeting market demand, but also that the income generated is distributed according to the market value of the marginal product of workers and other suppliers of

inputs. In Laborem Exercens, however, the claim for merit in human labor is based not on its market value but on its participation in the creative work of God.[4] Some distributional principles, such as, the principle of equal pay for equal work can be grounded in criteria of both rights and merit.

Various theories of economic distribution incorporate criteria of equality and freedom in varying proportions. Egalitarian theories of income distribution as they apply to international economics typically stress a commonality of human rights, including the minimal right to the means necessary for the satisfaction of some measure of basic human needs. Libertarian theories tend to emphasize individual rights associated with economic liberty, including ownership of property, rewards for entrepreneurial initiative and the personal and social benefits derived therefrom.

For a long time, domestic public policy in most countries, capitalist and socialist, has intervened in economic activity to achieve socially acceptable mixes of freedom, equality and growth. The tools are familiar, ranging from tax and transfer mechanisms and public expenditures for social purposes to public ownership of productive resources and regulation of prices, incomes and output. The international economy, however, has historically been subject to much less international public intervention of this kind. Hence, although domestic regulations obviously impose some constraints on freedom in international transactions, it is not surprising that international

inequalities are a major target of ethical evaluation of the economic relations between the developed and the developing economies of the world.

In 1981, for example, the developing countries of the world were inhabited by over three-quarters of the world's population, but accounted for only about one-fifth of the world's gross national product.[5] Expressed differently, the 1981 average per capita GNP in 143 developing countries of \$772 was less than ten percent of the \$8855 average in 29 developed countries, and only six percent of the \$12,530 average per capita gross national product (GNP) in the United States.[6] The inequality in the worldwide distribution of the gains from economic growth is even more noticeable in a comparison of the richest and the poorest. In 1981 the richest fifth of the world's population had an average per capita GNP of about \$10,000, close to 50 times the average for the poorest fifth of the world's people.[7]

Even if per capita growth rates in the developing countries were equal to those in the developed countries, the absolute gap in per capita incomes would continue to grow. However, the average annual rate of growth of GNP in the 73 lowest income countries of the world over more than two decades has been less than that of the 18 richest industrial market economies, thereby widening the gap both relatively and absolutely.[8]

Moreover, distribution of the gains from growth in past years obviously affects the composition of future output from the world's resources as well as the distribution of future gains

from growth. Present inequalities of income, for example, by determining the composition of future demand in both domestic and international markets help determine the share of the world's resources that will be devoted to the production of basic necessities and the share that will be devoted to other goods and services.

Thus, it is not surprising that Catholic social teaching from developing areas of the world, such as that in the Puebla documents, directs ethical criticism to the consumerist mentality that characterizes the societies of the richer nations.[9] It should also be noted, however, that international income inequalities also contribute to differences in public sector expenditures on social goods, such as public health expenditures, which are more than 30 times higher per capita in developed countries than in the developing world.[10]

Ethical evaluation of the economic relationships between the developing and the developed countries of the world is further complicated by the fact that both growth and future distribution are dependent upon distributional preconditions other than past shares in world output and income. Other distributional preconditions for international economic activity include the initial endowment of economic resources, which includes not only the obvious endowments of wealth, capital and natural resources, but also the size, growth, skills and education of the population. Distributional preconditions also include political conditions, especially those that determine who shall participate in economic

decisions concerning allocation and distribution and to what extent. The historical distribution of these preconditions for a long time supported a doctrine of comparative advantage in international trade that kept the resources of developing countries concentrated on the export of primary products to developed countries.

Finally, the distributional preconditions include cultural factors that influence economic activity. In some Eastern cultures, for example, it is more important to be in harmony with nature than to conquer and dominate nature. For Gandhi this principle also extended to setting limits on the fulfillment of material wants to which the human person should aspire.[11] In Western cultures, on the other hand, the ethical imperative to conquer and dominate nature goes hand in hand with the premise that material wants are unlimited, or at least will always exceed the capacity of existing resources.

Labor and International Markets

Much of the debate about the ethical quality of an international free market economic system overlooks the importance of assumptions about the economic, social and political preconditions that underlie and shape the working of market instruments and mechanisms. Thus, in a simple model of pure and perfect competition a market system left to its own devices tends towards a general equilibrium in which the remuneration of labor, like that of other factors of production, will be determined by the value of its marginal product, that is, the market value of the

added output of an additional unit of labor.

If all consumers and suppliers begin with an ethically satisfactory distribution of income, wealth and resources, and if they share the same knowledge about and access to the markets in which they function, and if none of them has sufficient resources, size, political clout or social status to control markets, then an ethically appealing equilibrium can be expected. For example, equal pay for equal effort and skills will prevail at every level of output everywhere in the system. All consumers will pay equal prices and none will pay a price more than the cost of production, including a competitive remuneration for the services of entrepreneurs.

The proper working of the competitive markets will insure that labor is fully employed and that new technology and more efficient forms of production and sale of goods and services will be brought on line as soon as the proceeds can be expected to outweigh the costs. There is a nice ethical dimension to the analysis that increases in productivity and the resulting economic growth will in the competitive model accrue either to workers in the form of higher wages or to consumers in the form of lower prices or better products or both. Profits and the return on capital, e.g., interest, beyond the minimums necessary to keep entrepreneurs motivated and the supply of savings sufficient for equilibrium growth will be non-existent or at most transitory on the way to an equilibrium in income and growth. All of this is ethically appealing, and suggests how economic growth might be

equitably transmitted through the international marketplace.

Of course, if, as in the developing world, there is surplus labor, that is, widespread unemployment and underemployment as a precondition, one of the major assumptions of the market model is violated, and the model will not work as predicted. Increases in productivity may raise the average product of labor, but the marginal product of employed labor, which determines wages, will not change. Increased productivity under these labor market conditions may of course, lead to growth-inducing increases in employment levels, but not to wage increases that are likely to narrow the gap in wage levels between rich nations and poor nations. This is the attraction of cheap labor in developing countries to international business. However, under conditions of surplus labor prevailing in developing countries market forces cannot be relied upon to transmit to worker incomes the value added in economic growth from increased productivity or increased demand.

Of course, the value added by improvements in productivity may still accrue to consumers in the form of lower prices. But if there is less than perfect competition in the markets for goods and services, that is, if any single firm or small group of firms can control or influence selling prices in some deliberate way, another crucial assumption of the competitive model is violated. This means that there is no reason to expect the gains from increased productivity to be passed along competitively in the form of lower prices to consumers.

Thus, free trade with the developing world makes it possible for the gains from improvements in developing country labor productivity to be retained in the form of profits and returns on capital beyond the necessary minimums, a social windfall for those whose incomes are derived from capital income. If these incomes are spent for the luxury consumer goods that are criticized in Catholic social teaching, there is little opportunity for workers in developing countries to recoup the value added that would have been theirs otherwise, even in a system operating within the assumptions of a well-behaved competitive economic model. This biased market behavior helps to explain ethical criticism in Laborem Exercens of contemporary "priority" of capital over labor in contemporary international markets.[12]

Of course, some of the non-competitive profits and returns to capital earned in the growth process may be reinvested in further growth-stimulating improvements of productivity. The hope would be that such improvements at least create new jobs, even if wage rates do not participate in the increased productivity. But even this is not assured, since the technology developed for economic growth may well be labor saving to reflect conditions in the labor markets of the most developed areas of the international market system.

However, the realities of international markets complicate the distributional effects of economic activity still further. For example, national barriers to factor mobility, that is, to international immigration, result in further deviations from the

norm of equal pay for equal work and skill. A taxi driver in Manhattan earns more than a taxi driver in Bombay, not because he works harder or is more skilled or more efficient in delivering his passengers. He earns more because his opportunity cost is higher, which simply means that he has better alternative employment opportunities than his Indian counterpart. He has better alternatives both because labor is more productive in U.S. markets and because, even in the absence of union or government intervention, U.S. labor is more likely to capture a larger share of productivity improvements in the absence of unemployment and underemployment at rates like those found in India.

Removing barriers to immigration would, of course, tend to equalize wages for comparable work in national markets. Illegal immigration, like that currently found between parts of Latin America and the United States, allows employers in the United States to appropriate at least part of the differential between foreign and domestic wages for comparable work because of the legal inability of the immigrants to compete equally in U.S. labor markets.

There is probably no moral or ethical principle that in the abstract fully justifies the disparities in incomes for comparable skills and work that currently exist among the nations of the world. However, nothing less than a radical conversion from short-term self-interest to unqualified commitment to a principle of universal human solidarity in the United States and other developed countries would make acceptable the social and

political destabilization that a radical reduction in barriers to immigration would create.

International Trade and Equity

The substitutes for immigration in spreading the gains from increases in economic productivity and growth internationally are found principally in international trade of goods and services and international capital movements, such as, direct investment and private loans through international capital markets along with various forms of capital transfer from official governmental sources. If workers themselves cannot move freely, the free movement of their products across national boundaries can in principle accomplish some of the same distributional effects. Using the doctrine of comparative advantage, any student of elementary economics should be able to demonstrate how the world's resources will be allocated optimally if countries try not to be self-sufficient in production, but rather specialize in producing those goods which they produce most efficiently. By exporting those goods in competitive international markets countries will earn the foreign exchange necessary to import the goods produced most efficiently by other countries.

If the assumptions of the competitive model are realized, this international division of production will utilize the world's resources most efficiently, that is achieve maximum world output. In addition, in theory free trade should equalize factor payments, that is, it should result in equal pay for equal work across national boundaries. Unfortunately for ethical evaluation

this result holds only under the assumption of full employment in all countries participating in the system.

Moreover, even the theory of free trade is ambiguous about how the gains from specialization will be distributed among the trading partners. Even the rigid assumptions of the competitive model do not rule out the possibility that one of the trading countries may capture all the increased income that results from specialization and trade according to the principles of comparative advantage.

The doctrine of comparative advantage was in its infancy a powerful analytic antidote to the inward looking trade policies of European mercantilist regimes. However, since World War II the less developed countries, especially in Latin America, have complained that the historically determined patterns of international specialization and division of labor are biased against the developing countries in their attempts to increase their share of world trade. Since 1950, for example, the share of the non-oil producing developing countries in the value of total world exports has declined from over 23 percent to just over 11 percent in 1980. On the other hand, the share of the developed countries of the free world in international trade, despite the post-1973 oil shocks, remained about the same.[13] Since 1970 the non-OPEC developing countries have maintained but not substantially increased their export share in the total value of imports by the developed market economies, while the share of their own exports directed to trade with each other has increased

by about 50 percent.[14]

It should be noted that the share of total exports of non-OPEC developing countries that goes to the United States, as well as the share of total United States imports that comes from these developing countries have both increased more rapidly than the comparable shares for other developed market economies.[15] Nevertheless, trade with developed economies remains an uphill fight for non-oil producing developing economies, especially as protectionist sentiment grows in the United States just as the developing countries are struggling to increase exports to earn the foreign exchange necessary to service the foreign debts that have accumulated so rapidly in the past decade.

In light of the urgency of basic needs for the majority of the populations in developing countries it is not surprising that ethical criticism is levelled at the composition as well as the excess of exports from developed countries to developing countries. The distribution of domestic income in developing countries, especially those with free market economies, is often as skewed in favor of a rich minority as is the international distribution of income among countries. Hence, consumer imports will tend to reflect the consumption preferences of the rich minority (which often resemble the tastes of their peers in the developed countries), rather than the basic needs of the majority. As a result it can be charged that producers of those goods in the developed countries, including workers, management and stockholders, benefit from the inequalities of distribution in

the developing countries. The often criticized consumerism of the developed countries both induces and feeds upon the consumerism of the rich minority in the developing countries.

It is also worth noting that international trade in military armaments during the 1960's and the 1970's increased at a rate only slightly lower than the rate of increase in total world trade.[16] Moreover, virtually all of the arms shipped in world trade come from the developed countries and the great majority of the shipments are to developing countries.[17]

Spokesmen for less developed countries often contend that a major reason for their failure to capture a larger share of world trade lies in the fact that primary products continue to dominate their exports. Despite decades of development and industrialization, the less developed market economies of the world still depended in 1980 on primary products for well over half their exports.[18] It can be argued that the prices of primary products in world markets are too unstable to be a dependable source of income for development. Thus, a price index of over 30 primary products (excluding oil) exported by less developed countries has gone through three cycles with fluctuations averaging 25 to 40 percent each just in the last decade.[19] The international demand for primary products fluctuates during recessions and booms in developed countries, whose business cycles are also tied to one another. On the other hand, supplies of many primary products in world markets are relatively unresponsive in the short run to changes in world demand. The gestation period for

coffee and cacao plantings are long, but once mature will be good for a large number of harvests.

In addition it has been argued that the prices of primary product exports of developing countries in world markets, especially of commodities from the tropics, where most of the less developed countries are located, tend to deteriorate over time relative to the prices of imports to developing countries from the developed world. The statistical evidence for this long run deterioration in the terms of trade for primary products of developing countries is hard to come by, partly because of the difficulty of separating out the effects both of export diversification and of the cyclical fluctuations in primary product prices mentioned above. Nevertheless, there is evidence that the terms of trade of the non-oil producing developing countries have deteriorated by over 18 percent since 1965.[20] This means roughly that, despite economic growth and diversification of exports from developing countries, a dollar's worth of developing country exports today purchases only about four-fifths as much as it did less than two decades ago.

The long run deterioration in the purchasing power of primary product exports is supported by the argument that over time demand in developed countries for primary products, especially for tropical products, will fail to increase at the same pace as income in developed countries. A doubling of family incomes in the United States, for example, is not likely to produce a doubling of consumption of bananas or pineapples. So too raw

materials from the developing countries constitute an ever smaller share of the total value of output in the developed countries as resource allocation in the high income countries shifts to the production of increasingly sophisticated goods. In addition, technological obsolescence has too often for comfort erased the market value of major primary product exports, e.g., jute in Bangladesh or nitrates in Chile.

Moreover, the conditions of the markets in which the primary product exports of the developing world are supplied differ from those in which the sophisticated manufactured products of the developed world are traded in ways that contribute both to short run price instability and to long run deterioration in the terms of trade, that is, the relative prices of exports versus imports, of the developing countries. The prices of primary products in world markets (with the obvious exception of oil) tend to be set competitively, that is, outside the control of individual suppliers.

Market conditions governing prices of many of the products that developing countries import from developed countries are, however, quite different. The markets for relatively sophisticated manufactured products are generally dominated by a handful of firms that are sufficiently large relative to market size that they can influence price. IBM surely has more control over the prices of its computers than Juan Valdes does over the price he receives for his coffee beans. In times of slack demand manufacturers of products with administered prices can respond by

holding firm on prices while cutting production where necessary to maximize revenues and/or profits. Juan Valdes has no such choice.

Furthermore, manufacturers with some control over the prices they receive for their products need not pass along the gains from improvements in productivity to the public in the form of lower prices. Instead they can retain those earnings for future investment or distribute the gains to stockholders as dividends or to workers in the form of higher wages, especially in labor markets where unions have adequate bargaining power. Thus, the competitive differences between the export and import markets in which developing countries trade discriminate not only with respect to price but also with respect to potential improvements in workers' incomes. Workers in developed countries have opportunities to share in some of the gains from growth in the developing world in ways that workers in that world do not.

Given these allocative and distributional problems associated with reliance on exports of primary products, it is not surprising that developing countries have sought to adopt alternative trade strategies. International commodity agreements have been formed among producers of primary products, e.g., coffee, tin and cacao, to give them some control over the prices and the quantities of product to be marketed in order to redress some of the short run instabilities and long run imbalances just described.

The success of export cartels, of which OPEC is the most

notorious example, depends partly upon the ability of the cartel to keep most of the world's production under its control. However, success depends also upon the willingness of importing nations to respect the cartel and upon the strength of demand for the product in the major importing nations. The United States imports roughly half the coffee produced in the world, so its willingness to live with an international coffee agreement is obviously important for the success of the agreement. Even then, however, the earning potential of the agreement depends upon the responsiveness of consumers to increases in price as well as upon the availability of acceptable substitutes. Even the strength of OPEC has not been immune to these influences.

For all of these reasons it is not surprising that developing countries have sought to diversify their exports in order to capture a larger share of growth in the world economy. They have sought to do so by moving into industrialization and away from specialization in the primary products which have been assumed to constitute most of their comparative advantage in world trade since the days of colonization by the more economically advanced nations. The path to industrialization in the face of a 200 year headstart by the developed world has not been an easy one for the developing nations. The lack of infrastructure, including transportation, communication, power and research and development capacity along with the absence of managerial and technical expertise have created bottlenecks that translate into inefficient, high cost production, not always offset by the

low wage costs of a surplus labor economy.

In addition, because the technology of modern production is often determined by the markets of the developed countries that serve the industrial preferences and needs of those countries, modern production processes are not always easily adaptable to the preconditions, social and political as well as economic, that exist in developing countries. Efficient low cost production in a developed country often requires a minimum plant size that is very large relative to resource availability and market potential in the developing country.

The requirements for capital and for management expertise to develop a competitive automobile facility, for example, can easily exceed the resource capacity of a developing country, while the marketing risks faced by a new exporter of autos can far exceed those faced by the dominant firms already in the industry. Moreover, concentration of a disproportionate share of a developing country's limited resources on a single major industry invests that industry with major impact upon employment, wages, political stability and other determinants of growth and the quality of life in the country.

Transnational Industry

Consequently, it is not surprising that developing countries have turned to the transnational corporations to plug them into the most lucrative industrial export markets of the world. Between 1960 and 1981 direct investment of United States firms in the industries of developing countries increased by more than 500

percent, from about 11 billion dollars to over 56 billion.[21] According to one estimate slightly over half the exports of manufactured goods and about one-third of all exports from Latin America to the United States in 1977 originated in subsidiaries of United States companies.[22]

Transnational industrial corporations bring to the developing countries investment capital plus modern technology, management and marketing expertise, direct and indirect employment opportunities, access to world markets along with new products for local markets, on-the-job training and other educational possibilities, as well as demand for the products of local suppliers and new sources of tax revenue for social expenditures.

These can be important features for economic growth and development, but are not easy to appropriate independently in existing international markets. In the absence of other institutional conduits the transnational firms become important transmitters of these elements. Moreover, unlike interest on foreign borrowing, which must be paid regardless of earnings, repatriation of earnings on direct foreign investments is not an issue until the investments are profitable.

The actual performance of each of these features in the development process of developing countries has, however, provoked serious criticism, including that found in Laborem Exercens and other recent social teaching of the Church.[23] Some of the criticism is directed at the cultural impact of the transnationals, especially upon traditional local values through the

import of aggressively materialist attitudes and standards and the introduction of consumer products deemed frivolous by local cultural standards of human needs, personal and social. The internationalization of consumption patterns, especially among the affluent minorities of developing countries contributes to a homogenization of material values that may be destructive to traditional spiritual values and culturally divisive and destabilizing in developing countries.

Much of the criticism is directed, however, at the interaction of the transnationals with factor markets, both domestic and international. It is frequently pointed out, for example, that capital movements of transnational companies are not dependable sources of development capital for individual developing countries because of the relatively high mobility of capital. The profitability of investments by transnational companies in developing countries is always subject to company reevaluation against profit opportunities elsewhere in the world, regardless of the long-term implications for development and employment in individual countries. There is little space or incentive in quarterly earnings reports to stockholders for corporate managers to justify non-maximizing behavior on social or ethical grounds.

Barriers to and social costs of free movement are obviously much lower for capital than for labor in international markets. These differences in factor mobility can be added to the distributional biases against incomes of workers in labor markets of developing countries described earlier as evidence for the "prio-

city" accorded to capital over labor in international markets that is criticized in Laborem Exercens.

Transnational companies can be expected to seek rates of return in developing countries higher than those in developed countries because of perceived political risks and uncertainties associated with foreign business activity. The desire of foreign firms for political stability also leaves them vulnerable to the accusation of complicity with authoritarian regimes that try to guarantee social peace by violations of human rights in the repression of local political dissent, especially among the poor. They may also expect higher operating margins to allow for fast write-offs of capital goods for the same reasons. Obviously, labor market conditions that keep wages low contribute to both these objectives and so are a principal attraction for foreign firms.

In addition, foreign firms seek the freedom to repatriate both capital and income (including that portion of value added attributed to rising labor productivity, but not captured in the wage rates of surplus labor economies.) They also frequently need the freedom to import necessary inputs not available locally.

These desires and needs obviously require foreign exchange and therefore put pressure on the balance of payments of the host country which is not necessarily offset by the foreign exchange generated by the export sales of the foreign firms. Lacking access to and a complete understanding of the internal accounting

procedures of transnational firms, developing countries are understandably critical of the prices they receive for the semi-finished products of local subsidiaries that are not sold on the open market, but are shipped to other divisions of the parent transnational for further elaboration. The prices recorded in the developing countries in such cases are obviously administered internally by the foreign firms, rather than set competitively in the marketplace.

By operating in markets that are not perfectly competitive in the domestic economies of both the developed and the developing world transnational business firms thus possess a degree of freedom that makes them international arbiters, not only of the international allocation of resources, but also of the distribution of some portion of the gains from international growth. In the surplus labor markets of developing countries, transnational firms can set wages either to share or to capture the gains from increased labor productivity. In the labor markets of the developed countries they can either pass along in wage negotiations some of the gains captured in the labor markets of developing countries, or they can use the existence of international wage differentials as a bargaining threat in union negotiations.

In product markets they can administer the prices of the output of their foreign subsidiaries as well as the prices of final products in ways that distribute the gains from growth differently among countries as well as between workers and consumers. The same is true of the distribution of fixed costs,

including depreciation schedules. Or they can do some of all the above. Their decisions are, of course, constrained by market expectations, domestically and internationally, as well as by social and political constraints, domestically and internationally.

Critical evaluation of the gains from technology transfer by transnationals to developing countries can easily reflect a Catch 22 spirit. The imported technology, for example, may be advanced and sophisticated. In that case it is also likely to be capital intensive, thereby putting pressure on the balance of payments of the host country for repayment of the capital import in scarce foreign exchange without assurance of commensurate benefit to domestic employment or labor incomes.

Or the technology may be relatively labor intensive, as in the transfer by transnational firms of only those parts of the production process that benefit substantially from cheap labor in the host country. Assembly of electronics components manufactured elsewhere, or handwork on textiles are frequently cited examples. In these cases there is in fact little transfer of technology for use by the host country. Even where there is useable technology transfer there are apt to be complaints about the foreign exchange burdens of royalties and license fees.

Transnational Banking

Since the oil crises of the 1970's the importance of direct investment by transnational industrial firms as a source of development capital has been challenged by petrodollar bank

loans. The non-oil developing countries have for a decade been on the receiving end of the recycling of oil producers' windfall earnings by international banks, especially those headquartered in the United States. By lending to developing countries some of the huge sums deposited by oil exporters the international banks helped to avert a possible international financial crisis occasioned by the sudden transfer of international financial resources to the oil exporters.

The international banks also recorded paper earnings in the process that were often more attractive than what was available in the recessionary economies of the developed countries. However, in the same process the developing countries accumulated debts that were also unprecedented. In the decade between 1973 and 1983 the medium and long-term international debt of the developing countries increased by over 500 percent, from 109 to 575 billion dollars.[24] Between 1970 and 1981 the international public debt of 13 major developing countries increased by a multiple of almost eight, from just over 31 billion dollars to over 227 billion.[25]

For many of these countries, especially in Latin America, payment of the debt service in hard-to-find foreign currency has taken precedence over national development objectives. At the insistence of international lenders and the International Monetary Fund countries like Brazil and Mexico have had to take domestic policy measures to reduce imports and increase exports in hopes of creating a trade surplus, that is, an excess of

exports over imports, sufficient to generate the foreign exchange necessary to meet annual debt service payments.

The policy measures prescribed, including devaluations and contractions of domestic money supplies, have resulted in additional severe unemployment beyond that attributable to chronic surplus labor, reaching over thirty percent of the labor force in some Latin American countries. Moreover, the resulting improvements in the balance of payments of the debtor countries have been less than encouraging. Despite their efforts to increase exports the debtor nations of Latin America in 1983 faced interest charges alone on foreign debt that represented 35 percent of their total export earnings.[26]

In the absence of formal default or moratoria, the balance of the debt service can be covered in the short run only by additional borrowing. This process of capitalizing interest payment defaults, along with additional high service charges by the lending banks for the privilege of "rolling over" the bad debts, creates high--and highly questionable--paper profits on the books of the foreign lending banks, while simply increasing the burden to the borrowers of the unpaid debt.

Additional lending, if it is forthcoming at all from banks in the United States and elsewhere, tends to be for shorter lending periods and at higher and fluctuating rates of interest. Developing countries argue that the desired outcome of their borrowing in the form of competitive exports for world markets requires much more time to generate the necessary conditions for

internal development and to remove inflationary internal bottlenecks to economic growth.

Dependency or Interdependence?

Some critics argue that the accumulation of competitive imperfections in international markets for labor, capital, goods and services along with the behavior of the transnational industrial and financial firms are cumulatively biased to create a self-reinforcing economic dependency of developing countries on the developed world. It is argued by some that the imperfect international markets for both products and factors of production are interrelated and self-reinforcing in such a way as to prevent the international economy from reducing the growth in economic inequalities between the rich and poor of the world. These arguments go beyond economic analysis of markets to identify social and political relationships that contribute to dependency. Attention is paid, for example, to the natural alliances that form among economic elites in developing and developed countries as well as to the sometimes less than savory links between international business and corrupt unrepresentative governments in developing countries.

Others retort that the growth of the international economy has resulted in global interdependence. The dependence of the United States and other developed countries on imported oil and the recent relatively rapid growth of United States trade with developing countries, including imports of manufactures, are cited as evidence of interdependence. So too is the stake of

many large United States banks in the continued solvency of the major debtor nations of Latin America.

It is also claimed by some that the failure of developing countries to grow more rapidly belongs more to failures of domestic organization and will than to biases in international markets. They point to the high, relatively non-inflationary growth rates of the Asian NICS (newly industrialized countries), namely, South Korea, Taiwan, Hong Kong and Singapore. These countries have achieved high growth rates largely through success in world markets and with reliance on transnational firms in production, trade and finance. And they have done so with a distribution of income and wealth that is probably less skewed than that of many less internationally involved developing countries.

About all that can be said conclusively in this debate is that the present interaction of domestic development and international markets is not functioning to narrow the development gap for the vast majority of the world's poor. The degree of dependence of any single country, however, is related to a host of cultural, social, political, economic and personal characteristics and relationships, both internal and external, that identify the historical development of that country. This is consistent with the perspective of Laborem Exercens, which perhaps more than earlier social encyclicals acknowledges a principle of pluralism of development models within the developing world, involving different mixes of market freedom and deliberate public intervention in the ownership and allocation of resources and in the

distribution of income.[27]

Policy Alternatives

The options for international economic policy are as varied as the analyses that support them. As indicated earlier, the international economy has been subject to less international regulation than most domestic economies, capitalist and socialist. Developing countries have responded unilaterally to their disadvantages in international markets with a variety of selective and sometimes conflicting restrictions on trade in goods, services and capital with developing countries, including tariffs, exchange controls and a plethora of regulations restricting the freedom of foreign investors.

At the same time, there are arguments for even greater liberalization of the international economy. These mostly have to do with the removal of protective tariffs and similar obstacles on grounds of efficiency in the allocation of the world's resources. Removal of protective tariffs in the United States on manufactures from developing countries would allow developing countries to earn scarce foreign exchange for development needs and for service on debts to developed countries that cannot be met without inflows of foreign exchange.

Free trade also helps keep prices low for consumers in the United States. However, because surplus labor in developing countries prevents the doctrine of comparative advantage from operating in accordance with the full-employment assumptions of the competitive market model, trade in actual practice can permit

developing countries to export some of their unemployment to the United States. This means that tariff removal would have to be accompanied by domestic economic and social policies, such as retraining programs and social subsidies to preserve equity as far as possible for affected United States workers. Even then it would be impossible to avoid interpersonal comparisons of the benefits to the poor abroad with the disruption of the lives of United States workers. The greater the disruption, the greater must be the acceptance of principles of common good and international human solidarity by those who currently benefit from the present system of international allocation and distribution.

Removing protective barriers in the United States and other developed countries, however, is not sufficient to redress the biased allocative and distributional effects of the international market conditions that have been the subject of this exercise, especially the existence in the developing world of surplus labor, imbalances in the mobility of labor, capital and technology as well as in relationships between markets for commodities and for manufactures, and non-competitive elements in the economic activities of the transnationals. Consequently, various proposals for deliberate intervention in the international marketplace have emerged in recent decades, and many of them, like commodity agreements, have been the subject of recommendations by six UNCTAD conferences over the past two decades with a limited positive response by the United States. The most recent UNCTAD conference has proposed a Common Fund to place a floor under

commodity prices intended to offset the deterioration in terms of trade of developing countries.

In markets for manufactured goods, developing countries have sought and received to some extent preferential tariffs for their manufactures which compete with those of the developed countries. Such preferences are justified on grounds that costs of production are high until both scale of production and efficiency increase to competitive levels. The burden of such concessions, to the extent that they are effective, falls selectively in developed countries upon competing producers, provoking political resistance or compensatory domestic concessions. Developing countries have also sought contractual agreements to permit more processing of primary products, especially of minerals, in their countries to capture more of the value added on the way to the final product. Oil refining, copper smelting and instant coffee processing are some obvious examples.

The international economy lacks the tax and transfer mechanisms that are available in the public sectors of domestic economies to redistribute part of the gains from growth in form of grants, subsidies, educational and social expenditures, etc. To some extent overseas development assistance by developed countries has acted as a substitute. However, as a share of their own incomes economic aid from the wealthiest developed countries has been far less than domestic social expenditures and income redistribution.

The United States, for example, spent about \$600 per capita

on public education but only about \$25 per capita in 1981 on official development assistance, which was less than the per capita aid expenditures of Canada, Japan and every western European nation except Italy.[28] The share of its gross national product spent by the United States on development assistance declined by about one-third during the 1970's (the development decade!), so that by 1981 only the Soviet Union among the major powers spent a percentage of its gross national product on development assistance less than the two-tenths of one percent spent by the United States.[29] On the other hand, military expenditures per capita in 1980 of \$632 in the United States were higher than for any other nation except Israel and four Arab oil nations.[30]

Slightly more than one-quarter of United States economic aid is channelled through multilateral institutions like the World Bank and the International Monetary Fund, which attempt to follow consistent, if not universally accepted, lending policies.[31] The remainder, however, is the result of bilateral political agreements and is spent principally on university consulting services and capital goods.

The interrelated character of international markets for labor, capital and final products and their imperfections is not likely to be well served by isolated policy options like bilateral trade and development assistance agreements. Consequently, there have been efforts to introduce more consistently planned and integrated sets of policy options to redress the cumulative

biases of international markets against the development of the poorest nations. These approaches to reform emphasize the interdependence of trade, aid, and markets for capital and labor within the world economy to achieve growth and distributional equity. Two notable examples of comprehensive schemes for reform of the international economy are the two Brandt Commission Reports, North-South: A Programme for Survival and Common Crisis: North-South Cooperation for World Recovery. These reports have called for an unprecedented level of international economic cooperation, including much greater reliance by individual nations on multilateral institutions for planning and coordination of the international economy. The Brandt Commission reports have received attention in Europe and developing countries, but have been largely ignored in the United States.

All of these policy proposals acknowledge the interrelationships of the international economy and attempt to make those relationships more equitable. All involve redistribution of some kind, whether only redistribution of future gains from growth or more fundamental redistribution of ownership and control of existing resources. All acknowledge the persistence of self-interest in international markets in policy recommendations that seek to reconcile conflicting vested interests, but increasingly the case is made for more global planning in the interest of the long-run peaceful survival of all of humankind.

The challenge of universal equity invariably falls most heavily on the developed countries. Therefore, recommendations

for domestic policy in those countries must acknowledge that international responsibility. It is on this point, for example, that the recent pastoral letter of the Canadian bishops, Ethical Reflections on the Economic Crisis is vulnerable. In seeking to find economic alternatives less dependent upon the United States the Canadian bishops opted for greater self-sufficiency based upon more labor-intensive production for domestic consumption, rather than upon development of high-technology export industries. In this context they recommend more production of textiles for domestic consumption.[32]

Unfortunately, they fail to note the implications of this recommendation. Either wages of Canadian workers will have to fall to keep the prices of Canadian textiles competitive with imports from developing countries, or prices will have to be allowed to rise. If they are allowed to rise, protective tariffs will have to be erected against cheaper imports from the developing countries to keep the Canadians employed. The net result will be higher prices for Canadian consumers and the export of unemployment to textile workers in developing countries. The ethical implications of economic interdependence are not so easily avoided.

The challenge of international equity to domestic policy in developed countries is perhaps nowhere more acute than in the United States, which, despite its own increasing dependence on the rest of the world, continues to dominate the world economy. As the recent world-wide recession has again demonstrated,

domestic economic policies in the United States reverberate throughout the international economy. We have not, however, been able yet to control our own federal budget, either by generating more tax revenues or by reducing military and other public expenditures.

Borrowing by the government to finance its huge budget deficits drives up interest rates. So too does tight control over the money supply by the Federal Reserve Bank to offset inflationary pressures from the budget deficit. High interest rates in the United States in turn raise the cost to developing countries of their foreign debt service, and attract international capital to the United States away from the developing and other developed economies of the world. As a result of these forces Latin American countries in 1983 became net exporters of capital to the United States and other developed economies in a paradoxical and burdensome reversal of conventional development theory.[33]

Inflation does inhibit growth. And growth in the United States increases domestic demand for exports and makes more palatable redistributive policy measures in behalf of the world's poor. It is not clear, however, that the poor of the Third World are beneficiaries of our decision to accept high interest rates as the price of maintaining non-inflationary high levels of defense spending and other public expenditures.

Moreover, it is unlikely that even enlightened individual self-interest alone will ever achieve the redistribution of income, wealth, control and power that is necessary to narrow

significantly the gap between the richest and the poorest of the world. Only a more deeply rooted personal conversion to universal human values of solidarity and a shared common dignity can embrace the scope of cooperative action that is needed for greater equity in international economic life, as Catholic social teaching right up through Laborem Exercens continually teaches. For the Christian that conversion ultimately rests on acceptance of the full implications of the Gospel message of creation and redemption in the love of Jesus Christ.

FOOTNOTES

1. Cf. Michael Novak, The Spirit of Democratic Capitalism, New York: Simon and Schuster, 1982), Ch. IX, pp.180-181 and P.T. Bauer, Reality and Rhetoric: Studies in the Economics of Development, (Cambridge: Harvard University Press, 1984), Ch. 2.
2. John Paul II, On Human Work: Laborem Exercens, (Washington: United States Catholic Conference, 1981), Ch. 6, pp.13-15.
3. Ibid., Chs. 4-5, pp. 11-13.
4. Ibid., Ch.25, pp. 53-56.
5. John P. Lewis and Valeriana Kallab, Eds., U.S. Foreign Policy and the Third World: Agenda 1983, (New York: Praeger, 1983), Table C-3, p. 220.
6. Ibid., pp. 219-220.
7. Estimates based on The World Bank, World Development Report 1983, (New York: Oxford University Press, 1983), Table 1, pp. 148-149.
8. Ibid., pp. 219-220.
9. "Evangelization in Latin America's Present and Future: Final Document of the Third General Conference of the Latin American Episcopate, Puebla de Los Angeles, Mexico," reprinted in John Eagleson and Philip Scharper, eds., Puebla and Beyond, (Maryknoll: Orbis Books, 1980), Sec. 213, Par. 56, p. 130.
10. Ruth Leger Sivard, World Military and Social Expenditures 1983, (Washington: World Priorities, 1983), Table III, p. 37.
11. For a commentary see Margaret Chatterjee, Gandhi's Religious Thought, (Notre Dame: University of Notre Dame Press, 1983), esp. pp. 117-119.
12. Laborem Exercens, Ch. 12, pp. 25-27.
13. Vd. UNCTAD, 1981 Handbook of International Trade and Development Statistics, p. 25.
14. Lewis, op. cit., Table E-4, p. 246 and Table E-7, p. 250.
15. Ibid., Table E-7, p. 250 and Table E-12, p. 256.
16. Ibid., Table E-1, p. 243 and Sivard, op. cit., Table I, p. 32.
17. Lewis, op. cit., Table F-4, p. 266.
18. Ibid., Table E-2, p. 244.
19. Ibid., Table E-8, p. 251 and Table B-4, p. 196.
20. Ibid., Table B-5, p. 197.
21. Ibid., Table A-9, p. 188.

22. Estimates based on data in ECLA, "Las Relaciones Economicas Externas de America Latina en los Años Ochenta," p. 39.

23. Cf. Laborem Exercens, Ch. 17, p. 39 and Puebla "Final Document," Ch. II, Par. 66, p. 131.

24. The World Bank, Debt and the Developing World: Current Trends and Prospects, (Washington: The World Bank, 1984) Table 1, p. ix.

25. Lewis, op. cit., Table B-8, p. 200.

26. ECLA, "Preliminary Overview of the Latin American Economy During 1983," Table 15, p. 37.

27. Laborem Exercens, Ch. 7, pp. 15-16 and Ch. 14, pp. 30-34.

28. Lewis, op. cit., Table G-4, p. 276 and Sivard, op. cit., Table II, p. 33.

29. Lewis, op. cit., Table G-4, p. 276.

30. Sivard, op. cit., Table III, pp. 36-40.

31. Lewis, op. cit., Table G-8, p. 280.

32. Episcopal Commission for Social Affairs, Canadian Conference of Catholic Bishops, Ethical Reflections on the Economic Crisis, section titled, "New Directions."

33. ECLA, "Preliminary Overview...", p. 5.

