

data are except by grubbing through the overly detailed literary description. And at the end we are unable to discern any systematic or consistent relationship among the variables or to advance our understanding of the processes of inflation and growth.

From Partition in 1947 through 1950, the government deficit (defined as the excess of expenditures over revenue financed by drawing down cash balances or borrowing at the central bank) fell from large to negligible. It was a period of inflation, inflation which was especially sharp in the first and last of the four years. But through it all the money supply (conventionally defined) was virtually constant. From 1951 to 1955 the government deficit rose from nothing (actually a modest surplus) to very large; the price level rose during two of the middle years, but it *fell* 12 per cent in the first and last years! The money supply was falling in the early part of the period and rising, at an accelerating rate, for the remainder. During the second-plan period, 1956-60, the government deficit consistently fell from very large to negligible; prices increased sharply at first, slower but consistently later; the increment to the money supply grew larger each year. And over the entire period gross domestic product sputtered ahead, never spectacularly. Similar, disparate changes occurred for the third-plan period up to the mid-1960's.

In short, there is no apparent systematic relationship between the values of the observed variables; the r^2 between any pair of variables must approach zero. Introduction of a "lag relationship" might lead to a higher measure of correlation. Or perhaps the divergence from expected relationships could be accounted for by introduction of other considerations. The author discusses the impacts of direct controls which were used from time to time, and he notes that for some years the balance-of-payments deficit, financed by drawing down foreign balances, was a factor. But oddly, the rate of interest and the role of private, as opposed to public, investment is never mentioned. Other variables readily come to mind.

In sum, from this book, we have some additional historical and descriptive facts—which is the major value of the book—but we have discovered no new insights into the basic problem at hand.

FRANK C. CHILD

Pakistan Institute of Development Economics

Trade and Trade Policy for Development by Staffan Burenstam Linder. New York; Washington; London: Frederic A. Praeger, 1967. Pp. xi + 179.

Linder's theme is that conventional trade theory, as set out in the theories of comparative advantage and the compatibility of internal and external equili-

brium, as well as the traditional free trade rules for trade policy are not valid for developing countries. He creates a trade model for developing countries in which internal equilibrium, in the sense of capacity income, and external (balance-of-payments) equilibrium are not compatible. Under these circumstances the need to satisfy the external equilibrium requirement dominates; this leads to a reduction of domestic output below capacity output. The existence of excess capacity in the midst of economic backwardness effectively retards continued investment and economic growth. Thus, the role of trade policy is to facilitate the achievement of capacity output.

Linder argues that it follows from his analysis that trade policies which relax the balance-of-payments constraint are desirable, even if conventionally wicked measures, like tariffs, quotas, export subsidies and various forms of discrimination, are adopted. This is so in spite of these measures leading to a misallocation of resources. Thus, the argument in this slim volume presumably provides a formalized and integrated rationalization of the systems of direct controls, differential exchange rates and bilateral trade agreements that seem so dear to officials in developing countries. My doubts about the correctness of the argument do not centre around whether the theoretical conclusions follow from the premises or whether the premises are reasonable. My doubts centre around the validity of the particular policy conclusions that the author has drawn from the formal theoretical arguments.

It seems to me that an alternative policy conclusion can be drawn from the analysis Linder presents. The constraints upon the operation of the external equilibrating mechanism which Linder assumes to exist are themselves the result of the prior adoption of a particular development strategy, modernization. The main policy thrust of the theoretical argument should be fed back as a critique of the assumed development strategy. That is, the major policy theorem that follows from the argument is something like: a development strategy of modernization undertaken without regard to the production capabilities of an economy or the foreign-exchange requirements of the production techniques adopted can retard growth. Modernization and industrialization should not be confused with and identified as necessary policies for accelerating economic growth.

For a developing country Linder asserts that both an export maximum and an import minimum (at capacity output) exist, with both exports and imports measured in an international currency. Nothing in the way of exchange-rate adjustments or equivalent policy measures can alter these maxima or minima. If the import minimum is greater than the export maximum then a foreign-exchange gap exists.

A portion of imports is input imports, needed to operate the existing plant and equipment at capacity and for the programmed net investment required to offset capacity-income savings. These input imports are assumed

inelastic with respect to the exchange rates—*i.e.*, essentially fixed proportions in production are assumed. If the input imports exceed the export maximum then an acute foreign-exchange gap exists. As a result, income must fall below capacity income and some *ex-ante* savings will be frustrated, the investment ratio will be smaller than it need be.

It follows that, if actual input imports are less than capacity input imports, any increase in the ability to import inputs will result in a multiple expansion of income. This is so because complementary domestic inputs can now be employed. There is a multiplier effect upon output from the import of these constraining inputs. Thus, there is a net gain to the world if non-input imports (luxury and consumption goods) are curtailed, if export subsidies that yield a net increase in foreign-exchange availability are introduced, and if foreign-exchange saving through allocation-distorting import substitution is subsidized. This is so because for a developing country, the expansion effect generated by high input imports more than compensates for the inefficiencies introduced by them.

It is easy to accept that a developing country, with a limited range exportables and often confronted with a world price for its major exports, faces an export maximum. It is not easy to accept that a developing country necessarily faces an input minimum.

Linder divides input imports into three classes: operation imports, re-investment imports, and expansion imports. Developing countries purchase their expansion imports, *i.e.*, capital goods, from developed countries. Furthermore, maintenance imports and particular types of operation imports are required from the country of origin to utilize expansion imports. Because of the limited set of production possibilities in a developing country, a considerable substitution of domestic for imported maintenance imports is not possible.

Thus, a conclusion that should have been drawn from the analysis is that a mere introduction of imported capital goods will abet development if the reinvestment and operation imports are small. Also development will in fact be retarded if these capital goods absorb too much foreign exchange. Simple machinery, whose maintenance is within the capabilities of the resources existing in the economy, is to be preferred to complex machinery, requiring imported inputs. The foreign-exchange cost of importing modern equipment is not a once-and-for-all cost. Hence, a continuing flow of foreign inputs may be needed.

Linder is aware of these points but chooses to ignore them after noting them. He notes the irrationality of the policy-makers' choice of techniques. He writes that, "[simple techniques].....using available domestic factorswould probably not impress policy makers as politically feasible, even

if methods of using capital goods that do not require advanced technology and could be produced at home were *in the end* to prove more effective (in promoting growth)" [p.15, Linder's emphasis] and "Yet it is noticeable that developing countries wish to use the most modern techniques in their investment programmes rather than simple techniques that could be introduced with domestically produced capital equipment" [p. 14]. But he does not conclude from this, as he should have done, that the adoption of production technique, without regard to the existence of domestic complementaries, may lead to a retardation of economic growth. Instead of drawing the above correct policy conclusion from his analysis, he proceeds to argue in defence of economic policies which may in the short run make the best of the earlier inappropriate choice of techniques without inquiring whether in the longer run, by distorting signals from the price system, these policies lead to further wrong choice of techniques. His policy recommendations may at best be considered temporary palliatives.

The existence of unused capacity because of the lack of imported inputs is quite common. Linder's argument correctly interpreted emphasizes the need to avoid this. The major policy issue is not a matter of making do with an inappropriate choice of technique, rather it is to set up criteria for choice of technique. Linder's introduction of the import requirements implied in a particular technique introduced into a particular economy is a step in the right direction, if it is interpreted as a constraint upon the choice of technique. It will be a step backward if the choice for technique is left to the prejudice of political decision-makers. I am afraid that, by showing how to make the best out of a bad situation, Linder's argument can become yet another obstacle in the path of the adoption of rational and successful policies for economic development.

HYMEN P. MINSKY

Washington University
St. Louis, Mo., U.S.A.
