Part I Adjustment and growth in the 1980s

2 The outlook for developing countries

World economic prospects have deteriorated since last year's *World Development Report* was published.

- The real price of oil is likely to be at least 80 percent higher in 1980 than in 1978. As a result, capital-surplus oil-exporting nations will run current account surpluses of around $110 billion this year and oil-importing developing countries deficits of more than $60 billion.[1] This prospect revives questions about the international financial system's ability to recycle enough funds—to industrialized and developing countries—to maintain import levels and economic growth rates. Furthermore, the real price of energy can be expected to rise during the 1980s.
- For reasons only partly connected with higher oil prices, the outlook for growth in the industrialized countries and in world trade has worsened. The widespread resurgence of inflation in 1979 and 1980 has prompted governments to take strong deflationary measures; the industrial economies are expected to show only sluggish growth in 1980 and 1981. This inevitably slows their demand for developing countries' exports. The 1980s are thus off to a slower start than anticipated a year ago.

Given these two developments, the world faces the need to adjust—to payments imbalances and expensive energy—on a scale comparable to 1974–75. But the adjustment must take place at a time when the outlook for capital flows —especially aid for the poorest nations—is worse than before. This adjustment will be spread over several years; while it lasts, the world economy and most developing countries are likely to grow more slowly than in the 1970s. Provided the adjustment is successful, a significant recovery should be possible from the mid-1980s onward.

Higher oil prices have clearly improved the prospects of those developing countries with oil to export, where a fifth of the developing world's population lives. Their GNP per person grew 2.8 percent a year in the 1960s, compared with 3.1 percent for the oil-importing developing countries; but in the 1970s the oil exporters accelerated to an annual 3.5 percent growth, while the oil importers slowed to 2.7 percent. (The disparity was even larger when GNP is adjusted for changes in the purchasing power of their exports —see box overleaf). With much increased oil revenues, at least for the first half of the 1980s, the oil exporters' growth will be constrained more by the productivity of domestic investment than by their ability to borrow abroad.

Adjustment for oil-importing countries

All oil importers, developing and industrialized alike, face a central challenge over the next few years—to adjust to higher oil prices and sluggish world trade while minimizing their loss of growth. They are subject to a formidable constraint: their ability to import more has declined, both because imports (particularly of energy) are more expensive and because the export outlook has deteriorated. These countries went through a similar adjustment in 1974–78, and there is much that can be learned from this earlier experience.

The adjustment process has two stages. First, when there is a sudden increase in the cost of imports relative to export earnings, countries squeeze imports—and so growth slows sharply. Because too sharp a fall is disruptive, both economically and politically, countries accept large current account deficits and finance them from borrowing or aid. During the earlier adjustment period the current account deficit of oil-importing developing countries rose sharply —from 2.3 percent of their GNP in 1970 to 5.1 percent in 1975; from 1978 to 1980 it went from 2.3 percent to 3.9 percent. Growth is falling off in these countries in 1980, but less sharply than in 1975 (see Figure 2.1).

The second stage is to reduce these current account deficits to levels that can be financed over the medium term. At the same time output and trade must be restructured to meet the new circumstances. This structural change requires heavy investment. New

1. See page viii for definitions of country categories.

GNP and trade prices

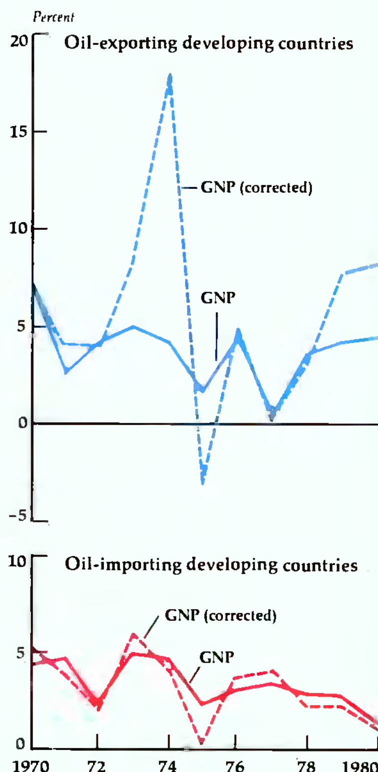
When a country's terms of trade shift substantially, changes in national product in constant prices do not accurately reflect changes in its purchasing power. The volume of imports that can be bought with a given volume of exports will rise if the terms of trade improve, fall if they deteriorate. There is no generally accepted way of measuring these changes in purchasing power; but a rough measure is obtained if export earnings are expressed in terms of the imports that they will buy—and any gain or loss is added to GNP.

Among the developing countries, the oil exporters and oil importers provide a vivid example of the difference such an adjustment can make to the apparent benefits of GNP growth. In 1974, the year oil prices rose most sharply, the oil exporters' output (as measured by their GNP per person in constant prices) rose 4.4 percent; but their "corrected" GNP rose 18 percent (see figure). That was exceptional: gains and losses from terms-of-trade changes are typically much smaller. But for the 1970s, the adjusted annual average GNP growth of 11 major oil-exporting developing countries was 2.4 percentage points higher than for 25 major oil importers, compared with 0.2 percentage points if the adjustment is not made.

Terms-of-trade effects are caused by a variety of factors: with the correction, the GNP of oil importers grew significantly more slowly than without it—in 1971, for example, long before oil prices rose. The reason was that commodity prices were depressed; two years later they were booming, and the correction augmented the growth rate.

Terms-of-trade effects on growth of GNP per person, 1970–80

(1977 prices)



energy sources must be developed and energy conserved, and in industrialized and developing countries declining or inefficient industries have to be replaced by competitive ones. So growth can pick up during the second stage, but it is still slowed by the continuing need for adjustment.

Slower growth compounds the political difficulties that can arise when governments pass on world price increases to consumers, particularly to politically powerful urban consumers, or cut back on public services. No less important, governments are concerned that rapid increases in the price of basic imported goods can cause severe hardships for the poor. These constraints can prolong the adjustment period. And there is a need to strike a balance between investments with a short-term payoff and those, such as infrastructure or education, which are vital for longer-term growth.

Judged against initial pessimism about their ability to adjust, the developing countries generally confounded expectations in 1974–78. In 1974 and 1975 their growth rates fell less than those of industrialized countries (Figure 2.1), helping to moderate the slowdown in world trade growth. Their adjustment was helped by substantial increases in official aid and other capital and by borrowing a significant part of the oil producers' recycled surpluses. Nonetheless, the result of these efforts was slower growth: in 1975–78, GNP per person in the oil-importing developing countries grew 2.3 percent a year—above the 0.8 percent in the 1975 trough, but still well below the 3.7 percent average for 1965–73. And some countries experienced serious fiscal and external debt problems. The poorest African countries were the biggest cause for concern; their GNP per person grew 1.6 percent a year in the 1960s, but only 0.2 percent in the 1970s. On average their people are as badly off at the end of the decade as they were at the beginning.

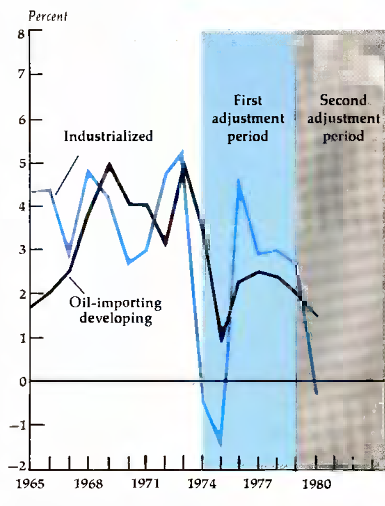
The oil-importing developing countries that coped best during the earlier adjustment period were:

- Those that reacted to the decline in their import capacity by a temporary slowdown in growth accompanied by a drive to expand exports. Import capacity (and hence output growth) was restored quickly. Most of these countries had grown rapidly and diversified their exports during the previous decade; a good example is Singapore.
- Those that, while maintaining import growth by foreign borrowing, used the borrowed funds mainly to sustain high levels of productive investment—including Brazil and South Korea.
- Those that benefited from good harvests resulting from improved agricultural policies and favorable weather (such as India) or rising migrant remittances (such as the Yemen Arab Republic).

Several of the developing countries that improved their economic policies and did well during six difficult years had previous records of slow growth and poor economic management: for them, improved domestic efficiency went a long way toward offsetting the effects

Figure 2.1 Growth of GNP per person: industrialized and oil-importing developing countries, 1965–80

(1977 prices)



of a deterioration in the world economy. And they are now much better placed to weather the current slowdown and recover in the 1980s.

The 1970s have shown that success in adjustment should be measured not just by the volume of recycling, or the share going to developing countries, or the reduction of developing-country deficits to affordable levels.These are all important, but they must be viewed in the context of the growth that the developing countries achieve. A key factor in that growth is the performance of the industrialized countries; in the 1970s their erratic growth and incomplete adjustment had a depressing effect on the oil-importing developing countries (Figure 2.1).

Adjustment in the 1980s

As in the 1970s, the adjustment required can be seen from both global and domestic viewpoints. Globally, the oil importers' deficits are the counterpart of the surpluses of the capital-surplus oil exporters. Although each oil-importing country has powerful reasons for wanting to expand exports and restrain imports, they cannot all succeed simultaneously while the oil surpluses persist. The attempt to do so through uncoordinated domestic deflationary policies (especially if augmented by protectionism) will slow world economic growth even more. Because of their weight in the world economy, the industrialized countries in particular should maintain import growth—recognizing that this may involve large payments deficits.

On the domestic front, adjustment in the 1980s should benefit from the knowledge gained from experience. Moreover, it is now apparent that higher real energy prices are here to stay; so there is more incentive to take the difficult steps necessary to conserve energy and to develop domestic energy production. A number of countries that were large oil importers in 1973 are now projected to come close to self-sufficiency in the 1980s (for example, Pakistan and Colombia) or be major exporters (such as Mexico).

Unfortunately, however, there are several reasons why this adjustment may prove more difficult for many countries than the 1974–78 adjustment was.

- Some developing countries did not adapt effectively during the 1970s, and ended up with high debt-service obligations or slower growth (and in some cases both). In addition, many countries now have less room than before to squeeze either energy consumption or imports without reducing growth. In some countries (India and Tanzania, for example) shortages of fuel have already impeded the transport of food and other key commodities.
- Oil surpluses could stay at a high level for longer—both because more conservative development programs among the oil producers may boost imports less rapidly than in the 1970s, and because the real price of oil is likely to rise, not fall as it did in 1974–78.
- The prospects for capital flows are less favorable. Official finance—including aid—which played an important role in 1974–75 is not yet responding to developing countries' needs; commercial borrowing is likely to cost more; and both borrowers and lenders are likely to be more cautious. In addition, more of what is borrowed will have to be used for repayments of principal and interest on old debt (see page 25).
- The industrialized economies face more serious difficulties than in the mid-1970s, when adjustment tended to be viewed as a phase from which they would quickly recover. But the growth of the 1960s and early 1970s has not been regained; and although their slowdown may not be as marked in 1980–81 as in 1974–75, no quick recovery can be expected.

The current economic malaise of the industrialized countries results from much more than higher energy prices. Inflation in some of them is running several percentage points above its peak in 1974; they have plainly decided that it must come down and stay down before rapid growth can be resumed, and that deflationary measures are the best way of achieving this. There are question marks, too, over their long-term growth potential. Productivity growth has slowed sharply: on average it increased 3.9 percent a year in 1963–73, but only 1.7 percent a year since 1973. This stems from a complex of factors—among them, incomplete adjustment to higher energy costs, sluggish investment and a mismatch of skills in the labor market—that cannot be rectified quickly or easily.

Overall, even with a well-directed policy response by all countries,

Table 2.1 Summary of prospects for growth

(average annual percentage growth, 1977 prices)

Country group	Population 1980 (millions)	GNP per person, 1980 (1977 dollars)	Growth of GNP (High case)		Growth of GNP per person				
						Low case		High case	
			1980–85	1985–90	1970–80	1980–85	1985–90	1980–85	1985–90
Low-income oil importers	1,133	168	4.1	4.6	0.9	1.0	1.3	1.7	2.4
Sub-Saharan Africa	141	186	3.1	3.8	0.2	–0.3	0.1	0.1	1.1
Middle-income oil importers	701	1,275	4.9	5.7	3.1	2.0	2.4	2.6	3.5
Oil exporters	456	753	6.3	5.9	3.5	3.0	3.0	3.5	3.4
Industrialized countries	671	7,599	3.3	4.0	2.4	2.5	2.5	2.8	3.5

Note: For more detail, see Table 2.8 and Table SA.1 in the statistical appendix to Part I.

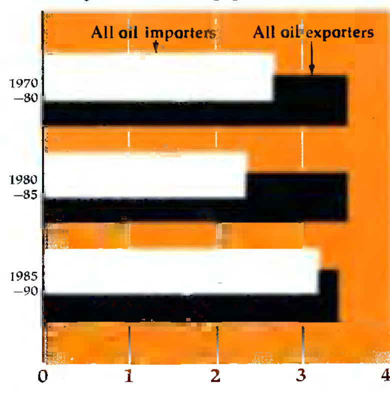
growth in the oil-importing developing countries is likely to be significantly slower in 1980–85 than in the 1970s—and still further below the average in the 1960s.

Key factors affecting growth: 1980–85 and 1985–90

To help analyze the outlook, two sets of illustrative projections have been prepared. Designated Low and High, they are based on alternative policy responses to current economic difficulties. Each scenario is internally consistent with respect to policies and outcomes. The Low case shows an unsuccessful adjustment in 1980–85; though payments imbalances are reduced, growth remains depressed, and inadequate foundations are laid for recovery after 1985. The High case represents a much more successful adjustment, with growth slowing less in 1980–85 and accelerating more thereafter (see Figure 2.2).

Figure 2.2 Developing countries' growth of GNP per person, 1970–90 (High case)

(average annual percentage growth, 1977 prices)



Because of the differences in growth rates between oil-importing and oil-exporting developing countries, estimates for them are shown separately (see Table 2.1). The projections of this *Report* are not directly comparable to those of last year's, but they represent a substantial fall in growth expectations for the oil importers over the next five years.[2]

The oil exporters have buoyant prospects throughout the decade (see Table 2.1). But the oil importers will grow more slowly in 1980–85 than in the 1970s, even in the High case; with a successful adjustment and a strong revival in world trade after 1985, their growth should accelerate in 1985–90. By contrast, their recovery would be weak in the Low case. Sub-Saharan Africa has the most disturbing outlook. Even in the High case, its growth in 1985–90 would be a meager 1 percent per person—far below the average for the oil importers; and in the Low case average incomes would actually be lower in 1990 than they were in 1980.

Whether the outcome will be closer to the High or the Low case will depend on the policies pursued by industrialized countries, the capital-surplus oil exporters and the developing countries themselves. At this early stage in the adjustment process, it is unclear how successful their policies will be in restoring growth, for the world as a whole or for developing countries. The estimates this year should therefore be treated with more than usual caution. But there are some disturbing signs that the seeds of the Low case are already being sown: on current prospects, aid for low-income countries is far from certain to meet the modest requirements of the High case, and some middle-income countries are experiencing both debt and political difficulties.

Thus, without a strong policy response during the adjustment period, the Low case is the likelier outcome. And a number of factors, including serious political instability, major problems in capital markets or a breakdown of world economic cooperation, could bring about a much worse outcome.

But the High case remains achievable—depending on policies in four key areas: the growth and structure of international trade; the changing pattern of energy

2. The projections of this *Report* differ from those of last year's for several reasons. For example, only two sets of projections have been prepared—a Low case, which is comparable to last year's Low case, and a High case, which is closer to last year's Base case than its High case. In addition, Iran and Iraq are now included among capital-surplus oil exporters; and improvements in data have led to revisions of some historical aggregates.

production and consumption; investment and productivity in the developing countries; and the inflow of capital. (A broader view of the determinants of economic growth—including the effects of human resources—is discussed in Chapter 4.) In each area, the emphasis is on what is required to increase growth; policy prescriptions are discussed in Chapter 3.

Table 2.2 Growth of exports and imports, 1970-90 (High case)
(average annual percentage growth rates, 1977 prices)

Country group	Exports[a] 1970-80	Exports[a] 1980-85	Exports[a] 1985-90	Imports[a] 1970-80	Imports[a] 1980-85	Imports[a] 1985-90
Oil-importing developing countries	5.6	5.7	6.8	4.6	4.7	6.3
Low-income	2.6	0.9	3.7	0.1	2.1	2.8
Middle-income	5.9	6.1	7.0	5.2	4.9	6.5
Oil-exporting developing countries	3.5	4.6	4.5	8.6	7.6	6.3
All developing countries	5.1	5.5	6.4	5.4	5.4	6.3
Industrialized countries	6.0	5.4	5.8	4.8	4.3	5.3
Capital-surplus oil exporters	2.7	1.8	2.0	21.1	10.9	7.3
Centrally planned economies	6.6	5.1	5.2	8.1	5.8	5.2
World	5.6	5.2	5.7	5.8	5.2	5.7

a. Goods and nonfactor services except for centrally planned economies, for which net nonfactor services are included as net exports.

International trade

With slow growth expected in the industrialized countries in 1980-81 and with much larger current account deficits for all the oil-importing countries, world trade growth will slow from the 5.5 percent a year it averaged in the 1970s. But if, as the High case assumes, the industrialized economies are able to average GNP growth of 3.3 percent a year in 1980-85—see Table 2.1—and if further protectionism is avoided, world trade could rise by an averge of 5.2 percent a year in 1980-85 (see Table 2.2). Thereafter, with the industrialized countries' GNP projected to grow 4.0 percent a year in 1985-90, it should accelerate. Exports of developing countries could expand at 6.4 percent a year in 1985-90, compared with 5.5 percent in 1980-85.

As with growth, the trade outlook differs sharply between oil exporters and oil importers—underlining the important effects of terms-of-trade changes. In the 1970s export volume for oil-exporting developing countries grew at about two-thirds the rate of that of the oil importers; but because the price of their exports rose so much faster, their import volume was able to grow twice as fast. For the capital-surplus oil exporters, the terms-of-trade benefits were even greater.

Although the terms of trade of the oil-importing developing countries are not projected to deteriorate markedly in the 1980s, exports will still have to grow faster than imports in 1980-85 to reduce current account deficits. But for low-income oil importers, and especially Sub-Saharan Africa, exports could grow more slowly in 1980-85 than in the 1970s—underlining their need for foreign assistance to maintain their import capacity. With a strong recovery of world trade in 1985-90, their export prospects would improve and export growth could exceed that of imports.

If the High case is achieved, the share of developing countries in world trade would increase from 20.1 percent in 1977 to 21.3 percent in 1990 (see Table 2.3). The structure of their trade could change more dramatically, with exports of manufactures growing about two and a half times faster than nonfuel primary exports. As a result, developing countries' exports of manufactured goods would rise from 24 percent of their total exports in 1978 to 39 percent in 1990 and from 10 percent to 14 percent of world manufacturing trade.

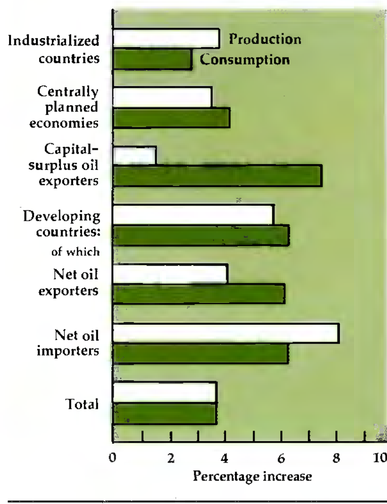
The biggest gains are likely to be in machinery and transport equipment (from 6 to 16 percent of developing country exports), in which Brazil, India and South Korea, for example, have become increasingly competitive in international markets. The developing countries' importance as markets for the industrial world would also increase: in 1978 they and the capital-surplus oil exporters already accounted for

Table 2.3 Percentage shares in world exports of goods and nonfactor services (High case)
(1977 prices)

Country groups	Primary commodities 1977	Primary commodities 1990	Fuels 1977	Fuels 1990	Manufactures 1977	Manufactures 1990	Nonfactor services 1977	Nonfactor services 1990	Total 1977	Total 1990
Developing countries	35.0	34.0	24.2	28.2	10.1	14.3	28.8	30.6	20.1	21.3
Industrialized countries	55.6	56.5	16.0	19.3	79.6	76.3	67.7	65.6	62.9	65.6
Other countries	9.4	9.5	59.8	52.5	10.3	9.4	3.5	3.8	17.0	13.1
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Figure 2.3 **Energy production and consumption growth, by country group, 1980–90 (High case)**

(average annual growth, million barrels of oil equivalent per day)



almost a third of North America's exports of manufactures, almost a half of Japan's and a fifth of Europe's.

Energy

Although uncertainty inevitably surrounds the prospects for new energy discoveries, the supply of energy is likely to remain tight during the 1980s. World production of primary energy from all (commercial) sources is projected to increase 3.8 percent a year over the decade (see Figure 2.3)—about the same as the industrialized countries' GNP growth in the High case, but considerably below that of the developing and centrally planned economies. As a result, real energy prices can be expected to rise further—though the rise is likely to be moderated and the energy constraint on growth eased if the industrialized countries achieve progress in both energy conservation and production (Figure 2.3 and Table SA.2 in the statistical appendix to Part I). The working assumption is that real oil prices will on average rise 3 percent a year.

For the industrialized countries, net energy imports (mainly oil, plus gas and coal) are projected to remain at some 20 million barrels a day of oil equivalent (*mbdoe*) throughout the 1980s. Among the developing countries, the oil exporters are expected to increase their energy exports by a third; some of today's oil importers either will be net energy exporters at some stage during the decade, or will have greatly reduced their energy imports by 1990.

But most developing countries will continue to import much of their energy needs. For all oil-importing developing countries, the "energy gap" under the High case is likely to widen from 5.6 *mbdoe* in 1980 to 6.3 *mbdoe* in 1985 (see Table SA.2). By 1990 the gap would have increased to 7.5 *mbdoe*, even if the countries succeed (as projected) in more than doubling production and restraining consumption growth. Their bill for imported oil for energy use (that is, excluding oil for such things as fertilizer production) would rise in nominal terms from $29 billion in 1978 to some $107 billion in 1985 and about $200 billion in 1990 (Table 2.4). Without a rapid expansion of exports and substantial financial support from abroad, they could find their growth severely constrained by the cost of energy imports. Individual country analysis suggests that oil imports as a percentage of export earnings will rise substantially for many countries from 1980–85, particularly among the low-income countries.

Figure 2.4 **Developing countries' savings and investment rates, 1960, 1980 and 1990**

(percentage of GDP, current prices)

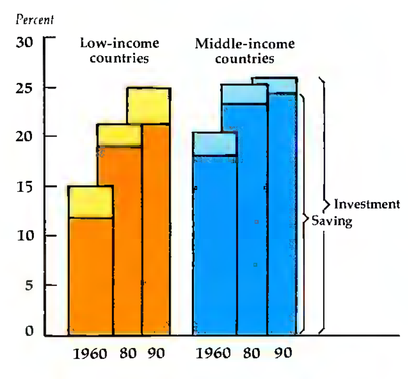


Table 2.4 Net imports of oil by oil-importing developing countries, 1975–90

Oil imports for energy use only	*1975*	*1978*	*1980*	*1985*	*1990*
Volume (millions of barrels of oil per day)	4.9	5.8	5.3	5.8	6.9
Low-income countries	0.4	0.4	0.3	0.3	0.4
Middle-income countries	4.5	5.4	5.0	5.5	6.5
Cost (billions of dollars)	22.1	29.2	57.8	107.2	198.0
Low-income countries	1.8	2.1	3.3	6.0	11.1
Middle-income countries	20.3	27.1	54.5	101.2	186.9
Price per barrel c.i.f.					
Current dollars	12.33	13.70	29.80	50.30	78.30
Constant 1980 dollars	19.60	17.13	29.80	35.10	40.85

Investment and efficiency

Developing countries have raised their savings and investment rates considerably in the past 20 years (see Figure 2.4). Further increases—and, still more important, improvements in the productivity of existing and new investment—can make a major contribution to adjustment and growth, as the experience of the 1970s has shown. Previous *World Development Reports* have discussed the importance of efficiency and policies for promoting it; Part II of this *Report* considers another important element in efficiency—the human factor.

The 1970s have shown which

measures can raise efficiency fairly rapidly. In agriculture, examples include balanced packages of irrigation, inputs of fertilizer and selected seeds, extension services and credit, and ensuring adequate producer prices. Efficient industrialization can be helped by policies that discourage undue capital intensity and do not protect domestic industry excessively. Many countries have learned from painful experience how to improve the efficiency of publicly owned enterprises and how to apply more rigorous economic criteria to project selection.

But even with greater efficiency, more investment would be needed to achieve the High case—especially in the low-income countries. They would have to raise their investment to more than 23 percent of output by 1985, and to 25 percent by 1990, matching the already high level of the middle-income countries. Some increases in savings rates are possible (see Table 2.5), although there are real limits to how far consumption in low-income countries can be restrained. But substantial increases in investment can be achieved only with more capital from abroad. For low-income Africa foreign resources will be required to finance about 40 percent of investment, and for low-income Asia 13 percent. By contrast, higher savings rates in the middle-income countries could reduce their dependence on foreign resources by 1990.

International capital flows

The analysis of trade, energy and domestic investment highlights the role that foreign capital must play in a successful adjustment by the developing countries. But the actual capital inflow will depend on both the needs of countries and on the likely availability and cost of capital from all sources (see discussion in Chapter 3).

Table 2.5 Developing countries' savings and investment rates, 1980–90 (High case)

(percentage of GDP, current prices)

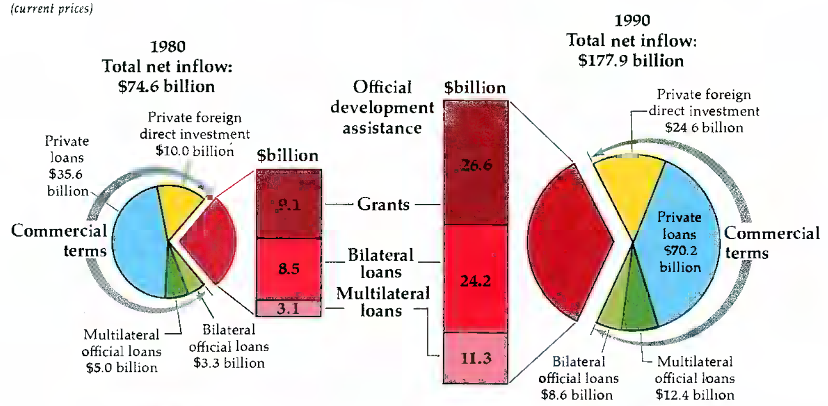
	Gross domestic investment			*Gross domestic saving*			*Resource gap*		
Country group	*1980*	*1985*	*1990*	*1980*	*1985*	*1990*	*1980*	*1985*	*1990*
Low-income countries	21.2	23.0	25.0	18.7	19.8	21.2	2.5	3.2	3.8
Africa	16.3	16.0	18.3	9.1	8.6	11.3	7.2	7.4	7.0
Asia	22.0	24.0	25.9	20.2	21.4	22.6	1.8	2.6	3.3
Middle-income countries	25.3	25.4	25.7	23.2	23.8	24.5	2.1	1.6	1.2
All developing countries	24.6	25.0	25.6	22.4	23.1	24.0	2.2	1.9	1.6

The projected pattern of net financing for all developing countries is shown in Figure 2.5. But the needs of developing countries for finance differ widely. Oil-exporting developing countries now look to be less dependent on foreign capital in the 1980s than was anticipated a year ago. Over the next five years, they can achieve High-case growth financed largely from their oil revenues. After running a current account deficit (before official transfers) of more than $10 billion a year in 1975–77, they could have a surplus of about $2 billion in 1980.

By the mid-1980s, however, the real value of oil export earnings is likely to be falling for some countries. If their imports are to rise to the level required for the High case, the oil exporters would have a current account deficit by 1985 of around $16 billion. To maintain their growth in the second half of the 1980s, they would need to borrow more heavily; their net private borrowing could rise from only $7 billion in 1985 to around $25 billion in 1990. Private capital would meet about two-thirds of their financing requirements in 1990 (see Table SA.6).

Figure 2.5 Net flows of medium- and long-term capital to developing countries, 1980 and 1990 (High case)

(current prices)



Note: Uses of medium- and long-term capital (billions of dollars) are:

	Oil importers		*Oil exporters*		*All developing countries*	
Use	*1980*	*1990*	*1980*	*1990*	*1980*	*1990*
Current account deficit before interest payments[a]	42.7	42.2	−11.1	30.2	31.6	72.4
Interest payments	18.3	62.0	8.8	17.5	27.2	79.4
Changes in reserves (net of changes in short-term debt)	−4.4	23.5	20.2	2.6	15.8	26.1
Total finance required	56.6	127.7	18.0	50.2	74.6	177.9

a. Defined as net imports of goods and services (except interest) minus private (but not official) transfers. See tables SA.6 and SA.7 in the statistical appendix to Part I.

Table 2.6 Current account deficits of oil-importing developing countries, 1970–90 (High case)

Country group	1970	1973	1975	1978	1980	1985	1990
	Current account deficit[a]						
	Billions of dollars, current prices						
Low-income	1.2	2.3	5.4	5.7	10.0	18.6	32.0
Middle-income	7.1	4.4	34.2	21.4	51.0	59.7	72.2
Total	8.3	6.7	39.6	27.1	61.0	78.4	104.2
	Billions of dollars, 1977 prices						
Low-income	2.2	3.2	6.1	5.0	7.1	9.2	11.8
Middle-income	13.2	6.0	38.3	18.5	36.1	29.5	26.7
Total	15.4	9.2	44.4	23.5	43.2	38.7	38.5
	As percentage of GNP						
Low-income	1.6	2.2	3.8	2.7	3.6	3.8	3.9
Middle-income	2.5	0.9	5.3	2.2	4.0	2.6	1.8
Total	2.3	1.1	5.1	2.3	3.9	2.8	2.1

a. Excludes official transfers.

For oil-importing developing countries the outlook is very different. Although their current account deficit in 1980 is smaller as a percentage of GNP than it was in 1975, in constant prices it is roughly the same (see Table 2.6). The low-income countries in particular face serious financing problems. To achieve High-case growth of 1.7 percent per person a year in 1980–85, their current account deficits would have to rise to 3.8 percent of GNP by 1985 (the same as in 1975) and would rise further by 1990. Since the low-income oil importers have only limited access to commercial funds (other than some short-term borrowing and suppliers' credits), deficits of this size can be financed only if:

- Aid from DAC and OPEC members trebles in current prices over the decade.
- Support from the multilateral institutions is increased correspondingly.
- The share of the low-income countries in bilateral aid from the industrialized countries increases to around 50 percent from about 40 percent at present.

This requires only a marginal increase in the aid performance of the industrialized countries—from 0.34 percent of their GNP in 1979 to 0.35–0.36 percent of GNP in 1985, then staying at this level. Unfortunately, aid prospects are not encouraging (see Chapter 3)—and this has serious implications for low-income countries. For example, the Low-case assumption for DAC donors—lower GNP growth, aid falling to 0.30 percent of GNP by 1982, with 40 percent of bilateral aid to low-income countries—would account for 0.3 percentage points of the difference in average annual growth for low-income countries between the Low and High cases.

For the middle-income oil importers, bilateral official finance is not likely to be as freely available for funding current account deficits in 1980–81 as it was in 1974–75. And lending by the multilateral institutions at market or near-market terms will depend on increases in the capital that backs their bond issues.

As for private finance, some countries that have borrowed heavily in the past and already have high debt-service obligations will need to be cautious about further borrowing. Given the High-case outlook for their current accounts, the debt-service payments of middle-income oil importers will peak at around 29 percent of their exports of goods and services in 1985 (see Table 2.7).

In the High case, private finance (including direct investment) provides a slightly larger proportion of the middle-income oil importers' net financing requirement in 1985 than in 1990, though smaller than in 1980 (see Table SA.7). If the Low case comes about, developing countries' export growth would fall more than their import growth—and hence they would remain about as dependent on nonconcessional finance as in the High case. If the necessary finance could not be obtained—because of concern about creditworthiness, for example—growth could slip even lower than the Low case, and the number of countries in serious debt difficulties would increase.

The extraordinary expansion of private commercial lending to developing countries that took place in the 1970s is unlikely to be repeated during the current

Table 2.7 Debt-service ratios of developing countries, 1977–90[a] (High case)
(percent)

Country group	1977	1980	1985	1990
Oil-importing developing countries				
Low-income	10.1	9.2	11.3	11.5
Middle-income	19.8	25.7	28.6	22.1
Oil-exporting developing countries	16.0	15.4	13.5	12.9

a. Interest and amortization payments on debt divided by exports of goods and services. Figures are from individual country analysis of 25 major oil-importing developing countries and 11 major oil-exporting developing countries.

adjustment; but the increases projected for the High case are not implausibly high. In nominal terms, net private lending to all developing countries would rise only 3.2 percent a year in 1980-85. This would lower debt-service ratios for oil exporters and slow their increase for oil importers. The 11 percent (nominal) annual rise projected for net private lending in 1985-90 would stem largely from increased borrowing by the oil exporters. Indeed, if major borrowers do adjust successfully in 1980-85, by building up their export base and earning good returns on capital invested, private lending may well rise more than is projected.

Regional growth in the 1980s

Whether the Low or the High case is achieved, most of the past decade's disparities in growth rates between different groups of developing countries can be expected to continue in both halves of the 1980s (see Table 2.8). There are too few oil exporters to identify systematic differences by region and income group in their prospects; but the aggregate figures for the oil importers hide wide differences.

With strong economic management, continuing agricultural progress and more aid, growth per person in low-income Asian countries could be substantially higher in the 1980s than in the 1970s. But it would still be well below that of middle-income oil importers, and in the Low case it would not be much more than 1 percent a year for the decade. The situation for low-income Africa is worse. These countries face a desperately hard adjustment period—coming on top of the economic stagnation of the 1970s. Even under the comparatively optimistic assumptions of the High case, their growth would be negligible in 1980-85. The plight of these poor Asian and African countries—particularly the latter—deserves special attention from the international community.

As they adjust to less buoyant export prospects and higher energy costs, middle-income oil importers can also expect slower growth—from 3.1 percent per person a year in the 1970s to a range of 2.0-2.5 percent during the first half of the 1980s. It would take the favorable international environment and successful adjustment of the High case for growth in the second half of the 1980s to exceed the average of the 1970s (and match that of the 1960s).

The slowdown in 1980-85 would be most marked in Latin America and the Caribbean—from 3.5 percent in the 1970s to 2.2-2.6 percent in 1980-85. Even with a strong recovery after 1985, growth for the 1980s could still fall below that of the 1970s. In East Asia and the Pacific there would also be a slowdown in 1980-85, and these countries too would not repeat their extraordinary growth of the 1970s. But they have made continuing progress in raising savings and investment rates, in expanding exports and in reducing population growth. As a result, they are likely to continue to achieve faster growth per person than any other region.

Growth in the comparatively high-income countries of Southern Europe has been slowing, and the trend could continue in the 1980s, since these countries are very dependent on oil imports and on trade with Western Europe. Some will join the European Community during the 1980s; the terms of their entry and how rapidly they adapt to membership will have a marked effect on their growth.

Finally, for the middle-income oil importers of Sub-Saharan Africa and the Middle East and North Africa, the slow growth of the past two decades seems likely to continue into the 1980s.

Table 2.8 Growth of GNP per person by region, 1960-90

Country group	Population, 1980 (millions)	GNP per person, 1980 (current dollars)	Average annual percentage growth[a]					
					Low case		High case	
			1960-70	1970-80	1980-85	1985-90	1980-85	1985-90
Low-income oil importers	1,133	216	1.6	0.9	1.0	1.3	1.7	2.4
Africa (Sub-Saharan)	141	239	1.6	0.2	−0.3	0.1	0.1	1.1
Asia	992	212	1.6	1.1	1.1	1.5	2.0	2.6
Middle-income oil importers	701	1,638	3.6	3.1	2.0	2.4	2.6	3.5
East Asia and Pacific	162	1,175	4.9	5.6	4.1	4.1	4.7	5.2
Latin America and Caribbean	256	1,775	2.7	3.5	2.2	2.4	2.6	3.8
North Africa and Middle East	30	667	−0.2	0.4	0.0	0.6	0.6	0.8
Africa (Sub-Saharan)	125	867	2.4	0.9	1.3	1.3	1.6	1.4
Southern Europe	128	2,950	5.4	3.2	2.2	2.2	2.5	3.4
Oil importers	1,834	751	3.1	2.7	1.8	2.2	2.4	3.2
Oil exporters	456	968	2.8	3.5	3.0	3.0	3.5	3.4
All developing countries	2,290	791	3.1	2.9	2.0	2.3	2.6	3.3
All low-income	1,310	245	1.7	1.7	1.2	1.8	2.1	2.5
All middle-income	980	1,521	3.4	3.1	2.1	2.4	2.7	3.4
Capital-surplus oil exporters	69	4,614	7.3	5.0	2.3	2.3	2.8	2.8
Industrialized countries	671	9,684	3.9	2.4	2.5	2.5	2.8	3.5
Centrally planned economies	1,386	1,720	n.a.	3.8	3.3	3.3	3.3	3.3

Note: More detailed information, including GNP and population growth rates, is in Table SA. 1 of the statistical appendix to Part I.
a. Calculated in 1977 dollars.

Compared with the industrialized countries, growth per person in developing countries will be slightly lower. The resultant widening in income disparities occurs primarily because of slow growth in the low-income countries and in the two slowest-growing middle-income groups. Research for this *Report* suggests that average growth per person of about 1.5 percent a year in low-income countries and about 2 percent in middle-income countries is needed to prevent the number of people in absolute poverty from rising. Thus, for these slow-growing groups (except South Asia in the High case) the extent of absolute poverty is likely to increase during the decade.

Policy implications by country categories

Given current policies, growth in oil-importing developing countries, with their total population of 1.8 billion, is likely to be unacceptably low. The steps needed to move toward, or beyond, the High case can be summarized by country group.

- For the oil-importing developing countries, faster growth depends heavily on economic management. This requires efforts to increase exports and investment, and to improve the efficiency with which existing and new investment is used. But increasing their import capacity and their ability to service debt will require buoyant export markets, and more capital from abroad.
- The oil-exporting developing countries can grow rapidly; but they must invest their oil revenues productively in the early part of the decade, and ensure that efficient production is encouraged in the nonoil as well as oil sectors of the economy. This will enhance their creditworthiness for the expanded borrowing needed to maintain strong growth after 1985.
- The capital-surplus oil exporters can contribute to efficient recycling by expanding their holdings of real and financial foreign assets, by avoiding disruptions in oil supplies or sharp price fluctuations, and by extending more direct financial support—concessional and nonconcessional—to developing countries. And they can help the developing countries to expand foreign earnings by buying more from them and by continuing to provide employment for their migrant workers.
- The industrialized countries can help by avoiding excessive deflation and by promoting technical and policy innovations to overcome structural constraints, thus encouraging a rapid resumption of sustained growth. They will assist developing countries (and themselves) by importing more from them; this requires trade liberalization as well as economic growth. The industrialized countries should reverse the tendency for their aid to fall as a share of GNP and should encourage prudent expansion in lending from their commercial capital markets to developing countries. The low-income countries in particular need more external financial support than is currently in prospect. The richer centrally planned economies also have the capacity to extend considerably more aid to developing countries and to expand trade with them.

What would be required for even faster growth?

It will take the kind of strong efforts discussed above to reach the High case. But that growth is itself low —measured against that of the 1960s and the first part of the 1970s, and by any reasonable expectations for development. Both for the world economy and especially for the developing countries, the potential exists for substantially faster growth. While the chances of exceeding the High case seem slim, it is important that all countries recognize the advantages—and the feasibility—of higher growth.

What would it require? One important element is more effective adjustment by the industrialized countries, particularly to higher energy costs. Another is a liberal trade environment, with less protection for products in which developing countries have an actual or potential cost advantage (this would help to reduce inflationary pressures). A third is more progress by all countries in producing and conserving energy, and some reasonable assurance that supplies would not be suddenly disrupted. Improvements in efficiency and some further increases in domestic savings in developing countries would also be valuable. Finally, capital flows to developing countries would need to increase substantially. Given increases in developing-country exports (and thus in debt-servicing capacity) and in the efficiency with which capital is used, developing countries would become increasingly attractive customers to commercial lenders. If the industrialized countries grew more rapidly, they would find it easier to provide more aid.

With good progress in all these areas, GNP per person in the developing countries perhaps could grow 4.3 percent a year in the second half of the 1980s (compared with 3.3 percent in the High case). This would mean growth of 3.9 percent a year in the oil-exporting developing countries, 3.6 percent in the low-income oil importers and 4.6 percent in the middle-income oil importers.

Achieving these results would require much more international cooperation than now seems likely. Aid of at least 0.5 percent of in-

dustrialized countries' GNP would be essential; still higher aid flows—approaching the 0.7 percent UN target—would raise growth further and help to reduce disparities between low- and middle-income countries. In addition, economic management would have to improve considerably. International efforts to encourage the steps required to increase growth—including those now being considered as part of the International Development Strategy of the United Nations—are therefore very much to be welcomed.

Broader implications of the projections

Since *World Development Report, 1979* was published, there have been major attempts to advance thinking and policies on development. The OECD study *Facing the Future* (Interfutures) was a result of three years' research on prospects for the global economy. The Independent Commission on International Development Issues (the Brandt Commission) published its findings in *North-South: A Program for Survival,* which called for bold reforms to avoid an otherwise grave future for international economic and political relations. The analysis of the present *Report* strongly endorses the Commission's emphasis on the interdependence—through trade, energy and capital flows—of all countries, as well as its emphasis on the importance of renewed efforts to reduce worldwide poverty.

There has been continuing, intense debate over an appropriate strategy for the Third Development Decade. But all agree on the need to raise the growth of the developing countries.

The advantages of higher growth are striking. To illustrate, Table

Table 2.9 Developing countries' GNP per person, 1980–2000
(1977 dollars)

Country group	1980	1985		1990			2000		
		Low case	High case	Low case	High case	Faster growth	Low case	High case	Faster growth
Low-income oil importers	168	177	183	188	206	218	215	261	311
Middle-income oil importers	1,275	1,408	1,448	1,585	1,719	1,813	2,009	2,423	2,843
Oil exporters	753	873	896	1,012	1,058	1,085	1,360	1,475	1,591
All developing countries	615	679	702	761	825	866	955	1,139	1,320

2.9 shows what would happen to GNP per person if the faster (than High-case) growth mentioned above could be achieved. Developing-country growth of about 1.9 percent above the Low case (and 0.9 percent above the High case) would start in 1985 and be maintained until the end of the century. The difference in growth may not seem large, but by 1990 for all developing countries it makes a difference of more than a seventh. By the end of the century, average real incomes with the faster growth would be almost two-fifths above those in the Low case and one-sixth above those in the High. And it is only with this sharp acceleration that growth of income per person in developing countries would match that of the industrial countries.

What does this growth mean for people's lives? The same method for estimating the link between income growth and poverty reduction used in the previous two *World Development Reports* suggests the following effects. In 1980 the number of people with incomes below the absolute poverty line is approximately 780 million. With the Low case this number would actually increase over the next decade to 800 million; in the High case it would fall slightly, to 720 million. If it were possible to achieve the faster growth mentioned, the number could fall sharply—to 590 million. The difference—reducing the number of people in poverty by between 60 million and 190 million during the next 10 years—is a powerful reminder of the benefits of higher growth. And as discussed in Chapters 4 and 5, growth in incomes is also vital for better nutrition, health and education, as well as for lower fertility.

The challenge of the decade

The world will reap great benefits from rapid growth. Without it, hundreds of millions of very poor people will live and die with little or no improvement in their lot. Many developing countries will find it hard to maintain political stability.

The developing countries face formidable obstacles on the way to rapid growth—many of which they will have to overcome themselves. But through their policies on trade, aid and other capital flows, the industrialized countries and the capital-surplus oil exporters have a striking impact on how much the developing countries can accomplish. Much will depend on the degree of international cooperation—which at present threatens to fall short of what is needed. For poverty, growth and political stability, the implications of the Low case—itself not the worst possible outcome—show that the world can ill afford such failures.