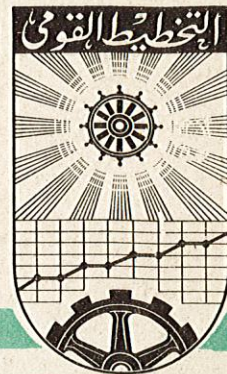


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THE APPLICATION OF THE THEORY
OF GROWTH IN SOCIALIST ECONOMY
TO DEVELOPING COUNTRIES.

BY

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THE APPLICATION OF THE THEORY OF GROWTH IN SOCIALIST ECONOMY
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The general conditions for socio-economic development in developing countries do not make it possible to present a universal type of growth adjustable to the needs of different groups of countries. But in spite of this, there is a necessity to determine some common problems of these countries to research the phenomena which regularly and continuously are existing in all developing economies.

One of the regular processes of development is the economic growth, conditioning to permanent increase of production and of consumption of the population, as well.

The economic theory should suggest the optimum solutions and forecast probable outcome of a policy of growth; the role of the theory consists in shedding light on the problems for the improvement conditions of the practical decision-making. So, within the limited scope of this paper are presented

the basic problems of the theory of economic growth, and especially the main relations between the process of growth and the factors determined its possible rate.

1. THE ECONOMIC GROWTH AND SOCIO-ECONOMIC DEVELOPMENT.

The contemporary economic theory in socialist economy differences two notions of great importance for analysis of the today problems of growth.

The first one is socio-economic development, on the second place we will present the notion described as economic growth.

The socio-economic development consists a wider sense. It means not only the growth of production or of the national income (as well as GNP), but consists within the problems of the structure of the economy, main changes in socio-economic structure of the population, the level of living of the population and improvements in it, as well as, the problems of the economic and social infrastructure of the country.

In other words - the economic development consists all changes in economy and in the social life of the country, evoking the general progress and technical improvements both in the sphere of production and in living standard of the people.

The way by which the socio-economic development may be achieved this is the way of economic growth. The economic growth is defined as the permanent growth of the national income (or of the GNP, as well), conditioned by the activity of main factors of growth. Within the process of growth we can observe changes in the relations between the factors, and as effect of them, the changes in general structure of the national economy.

Among the lot of factors conditioning the economic growth we can difference the direct and indirect factors.

The direct factors of economic growth may be presented as follows:

1. The increment of the employment in the sphere of material¹⁾ production;
2. The increase - of the productivity of work in the sphere of the material production;

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- 1) In marxist economy the national income is described as a result of the activity of the sphere of material production only. This sphere consists:
- industry, both mining and manufacturing;
 - agriculture, forestry and fishery
 - building
 - transport
 - Commerce - both home trade and foreign trade

3. the savings of productive equipment and means: machines, engines, productive buildings, instalations, means of transport and raw-materials, semi-manufactured products, materials, as well as, fuel, energy et cetera.

In fact the both factors 2 and 3 may be reduced to one because the savings of the productive means are the form of savings the labor inputs, so may be defined as an increase of the productivity of work.

The influence of these factors on the rate of growth we can present, as follows:

$$\Delta Y = L \cdot e + L_0 \cdot e_0$$

where: ΔY - denotes the increment of the national income

L - denotes the increment of employment in the sphere of material production,

e - denotes the increment of productivity of work in the sphere of material production;

L_0 - denotes the basic employment at the starting point,

e_0 - denotes the basic level of the productivity of work at the starting point.

After it's transposition the formula assumes the following form:

$$\frac{\Delta Y}{Y} = \frac{L}{L_0} + \frac{e}{e_0} + \left(-\frac{L}{L_0} \cdot -\frac{e}{e_0} \right)$$

The magnitude of the last part of the formula presented above, i.e. $\frac{L}{L} \cdot \frac{e}{e}$, is so small, that we can cut it out. So we will see:

$$\frac{Y}{Y} = \frac{L}{L} + \frac{e}{e}$$

Where: $\frac{Y}{Y}$ - denotes the rate of growth of the national income (we can denote it as),

$\frac{L}{L}$ - denotes the rate of growth of the employment (we denote it as),

$\frac{e}{e}$ - denotes the rate of growth of the productivity of work, (we denote it as),.

The following formula:

$$r = +$$

presents the rate of growth of the national income conditioned by direct factors of growth, i.e. the rate of growth of productivity of work plus the rate of growth of employment.

Besides the formula presented above, there is another formula, of great importance, very useful for exposition of the factors to economic growth.

It is, so called, investment, formula of economic growth, conditioned by indirect factors of growth:

productive investments, efficiency of investments and other factors.

This formula is very well known in world's economic literature as the "Kalecki's Formula" ¹⁾.

In the next paragraph of this paper we will present the model-formula very useful for explanation the relation between the rate of growth and the indirect factors of growth.

The possibilities to activate direct factors of economic growth are conditioned by the indirect factors in fact, because by the new investment objects it is possible to increase the increment of employment, and by the technical progress introduced into new into new investment objects, as a result of it, growth of the productivity of work may be achieved.

2. ASSUMPTIONS OF THE "KALECKIS FORMULA".

The analysis based on the "Kalecki's Formula" is highly simplified and includes the assumptions which are inherently linked with the exposition of the fundamental factors.

1) Professor Michael Kalecki was an world famous Polish Economist, author of many books and other works, among them very important is "The Outline of the Theory of Growth in Socialist Economy" published in 1963.

These assumptions we may present as follows:

1. In the material composition of the national income only two kinds of final products are taken into account: investment goods and consumption goods.

The gross national income is, thus, the sum of these goods:

$$Y = I + C.$$

2. The investment fund (I) covers exclusively the elements of gross productive accumulation comprised of gross productive investment and increase in the working assets in operation, indispensable to start production in new investment projects.
3. Non-productive investment, which contribute directly to the satisfaction of consumption needs, are considered on a par with other means of consumption and constitute a component of the total fund of consumption.
4. It is assumed that the level of capital intensity in sectors producing means of consumption and means of production is the same and, consequently, changes in the composition of investment do not affect the capital-output ratio.
5. It is assumed that the gestation period of investment projects,

by which we mean the period between the first outlay for the project and its first output in the form of increment of production, equals one year.

This means that the investments made in a given year will yield productive effects next year. An increase of employment in new investment projects takes place simultaneously with their putting into operations.

The rise of employment resulting from investment outlays is reckoned as a component element of these outlays.

The main assumptions of the formula presented above let us to analyse the main relations between the investment factors of growth, and their influence on the activity of the direct factors of growth. In this place of our analysis we did not assume the factors limited the possibilities to economic growth.

3. THE PRESENTATION OF THE "KALECKIS FORMULA".

The basic form of the formula written by M.Kalecki expresses a functional relationship between the growth rate of the national income on the one hand, and the rate of investment, the level of capital intensity and non-investment factors on the other.

The formula assumes the following form;

$$r = i \cdot \frac{1}{k} - a + u$$

Where: r - denotes the rate of growth of the national income in percent;

i - denotes the rate of gross productive investments together with the increase in the working assets in operation, in other words the share of productive investments in the national income ($i = \frac{I}{Y}$);

k - denotes the capital-output ratio, determining the inputs of investments per one unit of increase of the national income in the new investment projects (so, $k = \frac{I}{\Delta Y}$);

a - symbolizes the decrease of production (of the national income) in percent, as a result of negative effects of disinvestments (i.e. the decapitalization of existing productive capacities);

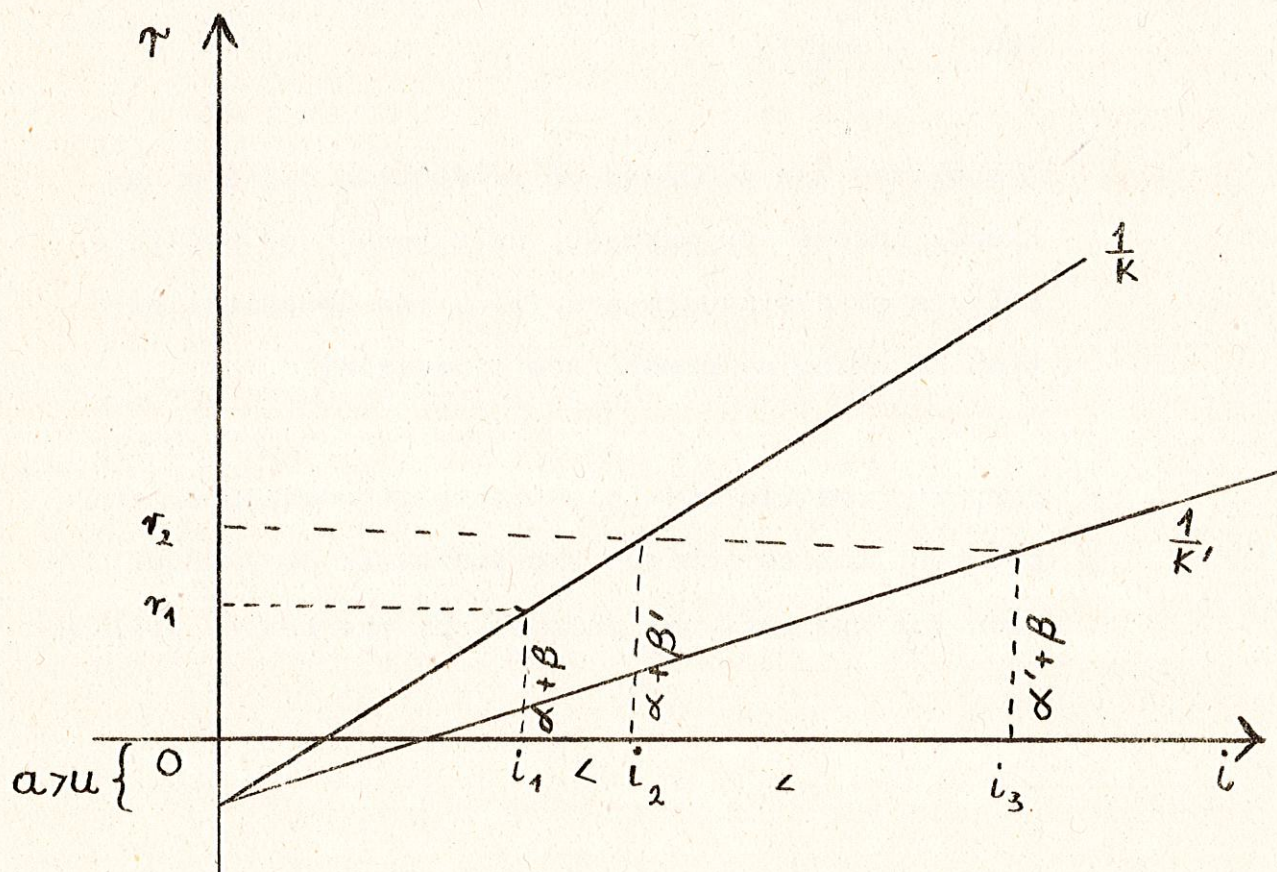
u - denotes possible non-investments improvements, in per cent let to achieve the increment of production (of the national income), by the better utilization

tion of the existing productive capacities.

In fact, this formula is a first degree linear function so we may present it in a graphical form.

Diagram 1.

The relationship between the rate of growth of the national income and indirect factors of growth.



On the axis of co-ordinates we present the rate of growth of the national income (r) and on the axis of abscissae we present the rate of gross productive investments (i).

We assume that the influence of disinvestments on the rate of growth is higher than the influence of non-investment improvements, so a u , and therefore the point in which the function begun is lower than 0. We assume, that this state that a u is constant to simplify our analysis and to limit it to the investment factors of growth only.

In the assumed conditions of the Kalecki's model-formula the changes in the rate of growth of the national income are determined by the changes of the rate of investments, as well as, ¹⁾ by the changes of the capital-output ratio.

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- 1) The changes of the capital-output ratio are conditioned by the general decisions of the choice of techniques and by the characteristics of the technical progress. The relations between the rate of growth of the technical equipment of labor (S) and the rate of growth of the productivity of work (e) result different possibilities of changes of the capital-output ratio (k). See: A. Muller, "The Theoretical Aspects of the Choice of Techniques Problem in Developing Countries". The Institute of National Planning . Cairo 1977.

On the diagram 1 we can see three different situations.

At first, the Basic Situation, when the rate of productive investments is equal to i_1 , and the capital-output ratio is equal to k (so, the efficiency of the investments is equal to $\frac{I}{k}$).

In presented conditions the rate of economic growth is r_1 and it should not change during the period when investment factors of growth would be not change, too.

The Second situation shown on the diagram presented the acceleration of the rate of growth. As a result of the decisions of the state, the rate of investments increases, and brings to effect the higher rate of growth. So, we can see that investments rate increased from i_1 to i_2 and as a result of it - the rate of growth increased from r_1 to r_2 . The capital-output ratio did not change so it is possible to assume that the techniques of production did not change too, and that the acceleration of growth was achieved by the acceleration of growth of the employment's rate. So, we can formulate in conclusion that the rate of growth r_2 is conditioned by higher rate of investments i_2 .

So, we compare this second situation to the basic one!

$$r_1 = i_1 \cdot \frac{1}{k} - a + u$$

or we can use the other formula:

$$r_1 = d + B,$$

and we can say, that

$$d + B = i_1 \cdot \frac{1}{k} - a + u.$$

The situation, when the acceleration of the rate of growth takes place, may be presented in such form:

$$r_2 = i_2 \cdot \frac{1}{k} - a + u$$

or

$$r_2 = \quad +$$

Where (it means, that the rate of growth of employment increased, thanks to building new working posts in new investment objects).

So if we compare both forms of the formula, we see:

$$i_2 \cdot \frac{1}{k} - a + u \quad i_1 \cdot \frac{1}{k} - a + u$$

or

$$+ \quad +$$

it means, that $r_2 > r_1$ thanks to the higher rate of investments results to accelerate the rate of growth.

The Third Situation presented on the diagram 1 is an accelerated rate of growth of the national income by way of acceleration the rate of growth of the productivity of work.¹⁾

This case takes place, when the supply of labor is limited and the needs to accelerate economic growth bring to effect necessity of introduction more intensive techniques into economy. As the result of it we can observe the increase of the capital-output ratio (it is : k k), so the efficiency of investments decreases ($\frac{1}{k}$ $\frac{1}{k}$).

Acceleration of the growth's rate from r_1 to r_2 ($r_2 > r_1$) under conditions of increasing capital-output ratio brings to effect increase of the investments rate from i_1 to i_3 (where $i_3 > i_2 > i_1$). So, the growth of investments rate in assumed conditions, when the rising of capital-output ratio must take place, must be higher too, than in conditions of constant techniques (it means: by the constant capital-output ratio).

1) To explain a functional relationship between the capital-output ratio and the productivity of work, see: A Muller, " The Theoretical Aspects of the Choice of Techniques Problem in Developing Countries". The Institute of National Planning. Cairo 1977.

4. THE APPLICABILITY OF THE "KALECKI'S FORMULA" TO DEVELOPING COUNTRIES.

Basing a model analysis on an investment formula seem a logical, with regard to developing countries, though it is an intentional simplification of argumentation. In reality, the process of socio-economic development is too complicated to be presented by a simple model only. On the other hand, such a model enables a separation of fundamental factors of growth, crucial to the rate of growth and its nature in specific socio-economic conditions, irrespective of the existence of a variety of other factors and incidence of multifarious forms of reality in particular countries.

The economic theory pays an ever increasing attention to a system approach to the analysis of the development processes.

The first question is, primarily, to emphasize the role of the state as a moving factor of the development. It is necessary to assume, that the state is the subject of economic activity of the paramount importance. It implements the policy of economic growth in order to secure a general socio-economic development, to overcome backwardness and to achieve a significant improvement in the level of consumption of the working population in the long-run.

The economic decisions of the state refer, first of all, to the public sector, but it is necessary to control by the state the economic activity of the private sector too.

The government must follow a policy of economic intervention, availing itself of the economic and non-economic means, which induce particular subjects to the kind of activity consistent with the intentions of the state.

Especially, the government must organize the control system of capitalists profits both within the country and in the sphere of foreign transfers to restrict the possibilities of the outflow of these profits abroad., The state's control system enables the use of the part of profits to advancement of the national economic goals the restriction of the exorbitant consumption of the propertied classes and the channelling of the flow of the private accumulation streams to the purposes designated by the state.

The other question is, secondary, to emphasize the role of social factors in the economic growth.

In highly developed countries labour qualifications are becoming one of the basic factors of growth. Very modern and high techniques utilized in these countries created the necessities of common technical education and training of the working people to use the technical means in optimum way. As the result of it the growth of

production may be achieved by the better utilization of the existing productive capacities. Under socialism the role of social conditions, human motivations and improvements in organization and management of economic activity is also taken into account..

In developing countries, however, and particularly so in those less developed and most backward, as a result of insufficiently developed productive capacities and the shortage of jobs, investments remain to be a primordial factor of growth.

The policy of growth in developing countries should realize two main goals:

1. increase of total production and consumption by permanent growth of the national income,
2. increase of employment to achieve higher level of production and to overcome the unemployment, particularly in overpopulated countries.
5. ECONOMIC GROWTH IN CONPITIONS OF OVERPOPULATED COUNTRY.

One of the most important problem in economic growth of developing countries is overcoming of the overpopulation and unemployment. This problem must be taken under studies from two

points of view.

On the one hand, this is the economic problem, because unemployment means that the productive possibilities of the man power are not fully utilized, so the level of the national income is lower than it would be achieved under conditions of full employment.

On the other hand, this is the social and political problem, for the reason, that all the people who want to work should have rights to do it.

The state in the overpopulated country may realize the policy of growth to achieve the full employment by the acceleration of the rate of growth of the national income. For this goal it is necessary to increase the rate of the investments and thanks to it-increase the rate of growth of the national income. The method of the acceleration of growth in assumed conditions should prefer to accelerate the rate of growth by the constant level of capital-output ratio.

The main cause of the existing unemployment is, that the rate of growth of employment is, and ever before, was, lower than the rate of growth of the man power supply.

We denote : α - the rate of growth of the productivity of work,
and we assume that it is constant, during all time
of our analysis;

- the rate of growth of the employment;
- the rate of growth of the man power supply.

So, the rate of economic growth we can express as follows:

$$r = +$$

by the assumption that

As a result of the presented situation there is unemployment within the economy, as a whole. Now, we will try to look forward to see the relations between the rate of growth of employment and the rate of growth of unemployment during the seven years period. We assume that the state achieved the possibility to grow up the employment at the same rate, as the growth of man power supply. We assume that the rate of growth of man power supply is equal to 3% per year; the previous rate of growth of employment was equal to 2% per year, and the present rate of growth of employment = . In the basic year t_0 number of employed workers is equal to the number of man power supply, and is equal to 1000000 of people.

Table 1.

The rates of growth of employment and
unemployment (hypothetical example)

Year	Employment		Man power supply		Unemployment	
	Number	Rate of growth	Number	Rate of growth	Number	Rate of growth
t ₀	1000000	2%	1000000	3%	-	-
t ₁	1000000	2%	1030000	3%	10000	-
t ₂	1040400	2%	1060900	3%	20500	205%
t ₃	1061208	3%	1092727	3%	31519	153%
t ₄	1093044	3%	1125509	3%	32465	3%
t ₅	1125835	3%	1159274	3%	33439	3%
t ₆	1159610	3%	1194052	3%	34442	3%

We can see, that equality achieved between the rate of growth of man power supply do not liquidate the problem. Even by state:

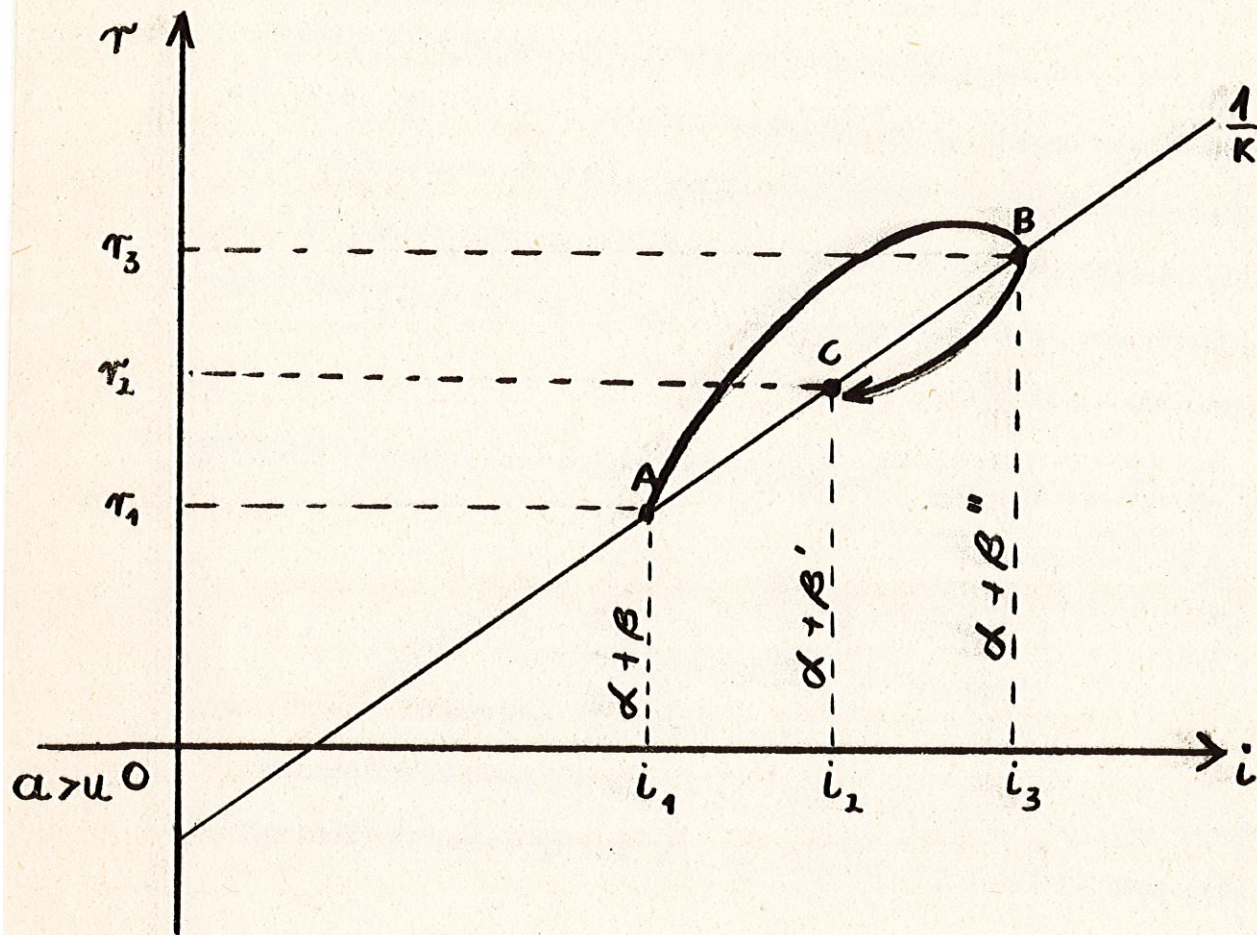
= , in connection with previously accumulated unemployment, thus the rate of growth of unemployment diminished to 3% per year, too but in long-term period we will observe permanent increase of the number of unemployment. Therefore the acceleration of economic growth ordered to liquidate unemployment must secure the rate of growth of employment at higher level than the rate of growth of man power supply.

The path of growth of employment compared with the rate of growth of man power supply should be as follows:

- The basic period
- The period of accelerated growth
- The final rate of growth of employment

So the rate of growth of employment must be in the period of accelerated growth higher than in the basic period, as well as, than in the final period of growth:

The path of the accelerated growth is presented on the diagram 2.



The diagram is designed under the same assumptions as the diagram 1. The points A,B,C, show the different rates of growth, according to the stages of accelerated growth.

The point B denotes the rate of growth in conditions, that , and by the highest rate of investments equal to i_3 , The rate of growth is equal to

r_3

This rate of growth may be held on only during the given period; after the exhaustion of man power reservations the rate of growth must diminish, according to the decreasing rate of growth of employment, i.e.

. Afterwards, by the given capital-output ratio, the rate of growth can be continuously held on at the same level, determined by the rate of growth of employment, which, at last, depends of the rate of growth of man power supply. Possibilities of the next acceleration of growth, in assumed conditions, would be achieve only by the increase of the capital intensity and according to them, by the increase of the productivity of work.

6. THE PROBLEM OF CONSUMPTION IN CONDITIONS OF ACCELERATED ECONOMIC GROWTH.

Acceleration of the rate of growth is conditioned by increase of the investments rate; in fact, it means changes in proportions between investment and consumption within the national income. If we assume that the national income is the sum of investments and consumption:

$$Y = I + C,$$

the investment fund would be equal to:

$$I = Y - C,$$

After transposition of the formula we can define the investments rate, i.e.

the share of productive investments in the national income:

$$\frac{I}{Y} = 1 - \frac{C}{Y}, \text{ or in other form:}$$

$$i = 1 - \frac{C}{Y}.$$

So, it is clear that when the investments rate invreases, in task to accelerate growth of the national income, the rate of consumption, (i.e. the share of consumption in the national income) must simultaneously diminish. In other words, ever the rate of investments rate increases, it is accomparied by the diminishing rate of consumption. The presented relationship between the two main components of the national income is of great importance from the social and political points of view.

Considering the nature of our analysis we shall confine ourselves to of such a dassification of the main goals/ accelerated growth which reveals current and future effect of growth within the time horizon assumed.

The first goal assumed by the state introducing policy of accelerated growth, is to increase the level of the national income in given time horizon. On the second place there is a goal, of great importance, connected with social policy of the state it is the increase of the rate of growth of the employment in task to liquidate unemployment and achieve full employment in the long-run,

But first of all, in this paper we assume that the subject of our analysis is a developing country the basic features of which being: the general aim of production, and of accelerated growth, of course, is to improve the living conditions of the population.

The assumption of this aim is tantamount to giving priority to maximization of the current consumption. But we can see that there is a contradiction between the aim of acceleration of growth and maximization of the current consumption.

The attainment of the maximization of the current consumption calls for adequately low level of investment and their appropriation to the branches producing the means of consumption. In consequence, the rate of growth will be presumably low and uniform, and the goal to liquidate unemployment will be achieved in such a long time horizon that it can be not taken under review.¹⁾

The aim of economic strategy of growth must consist both goals; acceleration of growth and increase of consumption, so, it must to attain a higher level of consumption in the long run. The task of primary importance is the creation of the productive base by means of expansion of the sector manufacturing the means of production. This calls for an acceleration of the rate of growth of the national income by way of increasing the rate of investment, which brings about a fall in the rate of consumption and slowing down of its rate of growth.

1) In fact, an acceleration of growth may be envisaged, if sufficiently strong stimuli, connected with external factors of growth, do occur. It did happen in practice when the country achieves a considerable increase of income from accrued export benefits, resulting from a sweeping increase in prices of its major export goods.

The higher rate of growth of the national income, the rate of investment being stabilized later at a certain level, results in an acceleration of the rate of growth of consumption and its absolute increase to such a level which could not have been achieved without the acceleration.

In the process of choice of strategy of growth there is necessary to applicate specific combinations of extensive and intensive factors of growth. The mutual relations of these factors, derivative of the investment decisions of the state, are conditioned by the investment possibilities of the economy and the balance of the labor force.

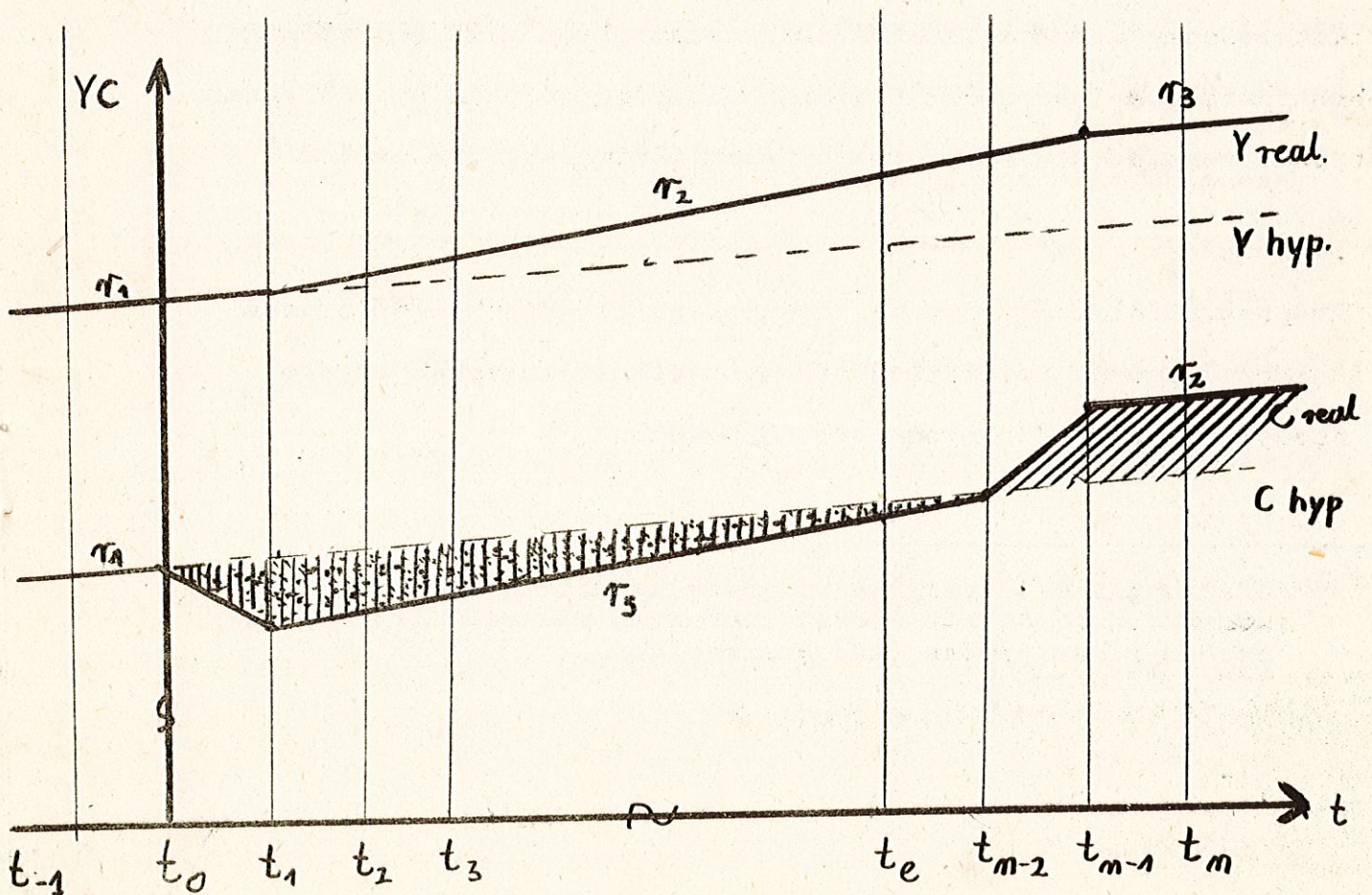
Assuming that the general aim of growth is to rise the level of consumption, the problem of choice of the rate of growth, capital-output ratio remaining constant, boils down to the answer to the following questions:

When the acceleration of growth will result in the long-term increase of consumption in relation to the level of consumption possible to achieve under a steady rate of growth.

We can observe the process of growth of the national income and of the consumption on the diagram 3.

Diagram 3.

The rate of growth of the national income and of the consumption in conditions of accelerated growth.



On the axis of co-ordinates we present the level of the national income and the level of consumption and on the axis of abscissae we present time in which the process of acceleration takes place.¹⁾

Under given assumptions, the increase of rate of investment results to accelerate the rate of growth, and in consequences - to diminish the level of consumption. After the time $t_l - t_e$ thanks to acceleration of the consumption - its level will be equal to the level of hypothetic consumption, which would be achieved at that time without acceleration of growth.

In the long-term the benefits in consumption will be achieved but for these benefits the population had to paid by the lower than possible, level of the consumption during the period $t_l - t_e$.

The problem of the size of consumption both in the short and in the long run constitutes the subject of analysis of the theory of economic growth of M.Kalecki.

1) This diagram is designed in semi-logarithmical scale for express not only the level, but also the rate of growth, both-national income and consumption.

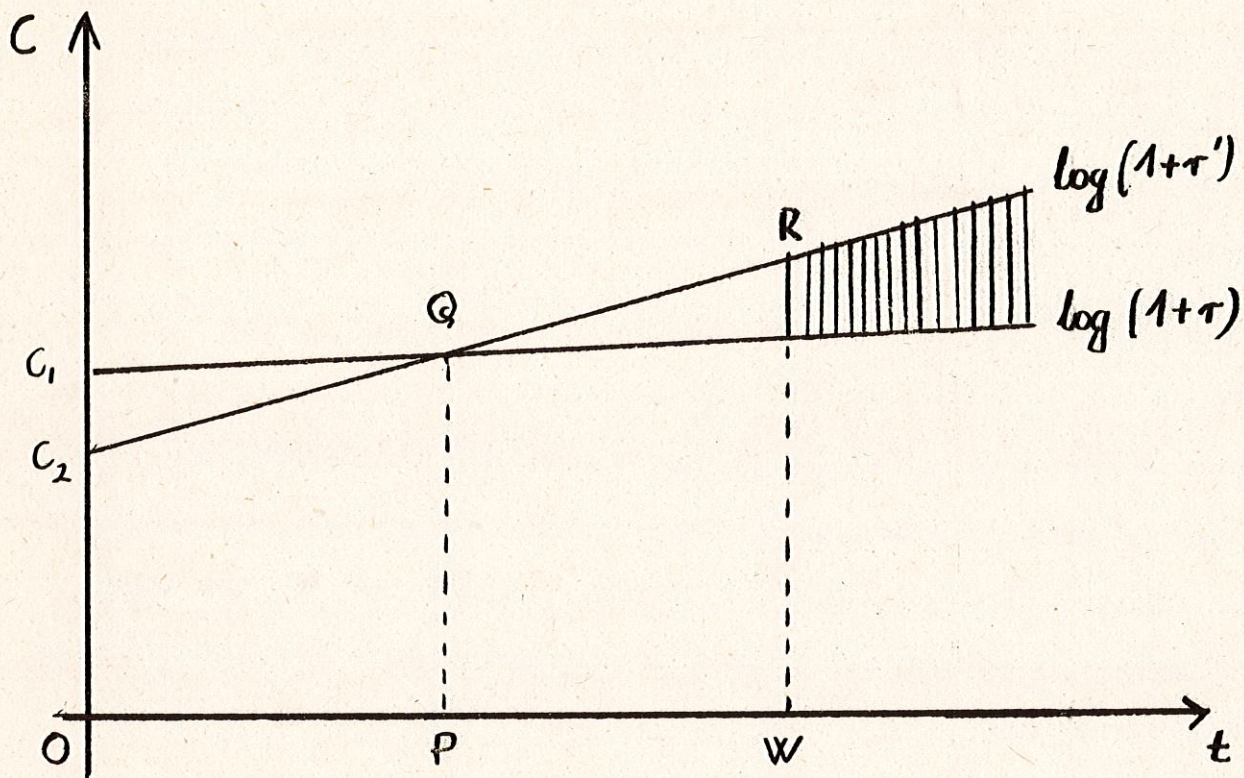
If we examine an alternative of steady or accelerated rate of growth, the capital-output ratio being constant, we shall arrive at a conclusion that with a steady rate of growth the level of consumption during a certain period of time will be higher than the level of consumption in the variant of accelerated growth. However, the rate of growth of consumption during the accelerated growth will be bigger than in the alternative variant, and as a result, after a certain time, the level of consumption corresponding to the accelerated growth will not only equal that corresponding to steady growth, but will also exceed this level.

Later on, in the long run, the level of consumption resulting from accelerated growth will be higher than the level which could have been achieved if the acceleration had not been initiated. The differences in the respective rates of growth will result in widening of the gap between the levels of consumption in both variants.

The graphic presentation of the above described process, in different form than on diagram 3, is presented on the diagram 4, which illustrates the consequences of the acceleration of growth from the point of view of consumption.

Diagram 4.

The rate of consumption growth under a steady and an accelerated growth of the national income.



On the axis of co-ordinates we present the level of consumption and on the axis of abscissae we present time in which the process of acceleration takes place. If the acceleration of

growth did not occur, the consumption would grow at a steady, rate, reaching in consecutive years ever higher level, which process is being illustrated, by the curve C_1 . The rate of growth would equal $\log (1+r)$.

The acceleration of the growth rate of the national income is conditioned by an increase in the rate of investment. The result of this would be a decline of a share of consumption in the national income and, consequently the level of consumption in the accelerated variant would be lower than in the alternative one (see also: on the diagram 3, - the period to $-t_1$). This is illustrated by the curve C_2 . The rate of growth of consumption in accelerated variant, however, is higher and equals $\log (1+r')$, that is the gradient of curve C_1 in relation to the horizontal axis t . During the period OP the consumption in the accelerated variant is lower than in the steady one (see also: the period $t_0 - t_e$ on the diagram 3), this being illustrated by the fact that the corresponding part of the curve C_2 is situated below that of C_1 . As a result of accelerated growth of both income and consumption the latter reaches in point Q the level equal to that of the alternative variant (it is corresponding with time t_e on the diagram 3).

Point Q , achieved after time OP , presents the year of equalization when the level of consumption in both variants is

equal. In subsequent years the curve C_2 will be permanently above the curve C_1 and, owing to the higher rate of growth in the accelerated variant, the gap between the levels of consumption will continue to widen. The area between the curves C_1 and C_2 in the section OP represents a relative loss in current consumption, suffered by the society in order to achieve future long-term benefits in consumption. The time of suffering lower consumption extends to the year of equalization at point Q. To the right of point Q a period begins when relative losses in consumption suffered during the period OP are compensated.

It is necessary to observe that the problems of long-term benefits in consumption is often subject to erroneous and excessively optimistic interpretations. For one thing, it is deemed that the possibility of rising consumption above the level which could have been achieved without acceleration, ensures the compensation for the foregone current consumption. It seems that the problem can not be confined to quantitative elements only. The consumption relinquished today can not be compared with the consumption recovered tomorrow.

Renouncing part of the consumption, at a time when its level is low, is much more painful to the people than an additional increase of consumption is rewarding, at a time when its level is higher.

The protracted period of consumption limitation along with the unmet expectation of the public as to the increase of consumption, may create wide-spread negative motivations, proneness to negation and disbelief in the ultimate success of the programme of growth under realization.

In developing countries, plagued by strained food balances, low level of incomes, difficulties in foreign trade, and the lack of sufficiently strong organization of social life, the realization of the policy of accelerated growth for a prolonged period threatens to aggravate all the above mentioned difficulties,.

