THE ROLES OF GOVERNMENT AND BUSINESS IN NATIONAL ECONOMIC DEVELOPMENT*

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The resurgence of interest in the problems of economic growth since the Second World War has brought important changes in emphasis in both theoretical and applied economics. For a long time, economic theory was confined largely to static equilibrium analysis and economic policies were directed mainly towards achieving balance among certain important aggregates, such as income and expenditure, employment and labor supply, and externally, international payments. The interest in economic growth has made these traditional concerns inadequate, for the study of economic growth is essentially a study of change; and change is a dynamic process. A great deal of recent advances in economic theory can be traced back to this rediscovery of the growth problem. We are not concerned here with these developments on the theoretical level, but with practical changes in economic policy. Specifically, the change in emphasis has reopened the important and basic question of the role of government -- and this necessarily means the role of private enterprise also -- in economic activity.[1] This question is crucial to an understanding of the practical aspects of the universal effort to achieve economic and social development and to secure a better life for people the world over. It will also serve as a point of departure for examining development planning which has now become a basic tool of governments in both developing and developed nations. In case anyone should raise an objection to the last statement, let me point out that among developed countries, only two do not practice some form of formal planning. These are the United States and Western Germany. And in the case of Western Germany where public investment accounted, over a long period, for over 40% of total investment, the lack of formal planning is a matter of semantics rather than substance.[2]

I. Need for Public Intervention

In order to examine the question of the roles of government and business in national development, I think it would be convenient to start by considering briefly the question of the need

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1 For a brief but useful examination of the basic question of the relationship between government, society, and economic development, see: Edward S. Mason, "The Role of Government in Economic Development," *American Economic Review*, Vol.L, No.2 (May 1960), pp. 636–41.

2 Albert Waterston, *Development Planning : Lessons of Experience*, (Baltimore : The Johns Hopkins Press, 1965), ch. III. See also : Geoffrey Denton, Murray Forsyth, and Malcolm Maclennan, *Economic Planning and Policies in Britain, France and Germany*, (London: George Allen & Unwin, Ltd., 1968), ch. II.

for public intervention in economic affairs. In other words, the first question we should consider is simply this: Why not leave everything to the market? We shall discuss this question from two angles, firstly, from the point of view of society as a whole, and secondly, from that of private enterprise itself.

From the point of view of collective welfare, it can be said that the market, while a powerful and indispensable allocative mechanism, is not quite adequate because of certain basic limitations. Let us first examine briefly these weaknesses on theoretical grounds and then go on to tie these observations to conditions in the real world. According to classical doctrine, the free play of the market will in itself lead to an optimization of national income, provided:

a) that there is perfect competition,

b) that we disregard the ethical problem of income distribution, and,

c) that we ignore "special" cases of increasing returns.[3]

Under such conditions, if each individual in society seeks to maximize his own benefits, the individual actions will automatically lead to a maximization of collective benefits also. This is the gist of the famous argument about the invisible hand unerringly guiding the collective destiny of nations. The operation of the economic system is best left to the free play of the market, with the role of government limited to that of keeping internal law and order and providing protection against external dangers and encroachment.

If things were as simple and straightforward as the classical model indicated, then it would be clear that governments should not interfere in economic matters. Since collective benefits are already maximized through the operation of the market mechanism, actions by government will, at best, add nothing to the welfare of the nation. And since government, like all human institutions, is not perfect, public intervention would only lead to a reduction in the welfare of society as a whole. Unfortunately, the situation is not as simple as the one outlined above. Even if we concede, for the moment, the "heroic" assumption that there is perfect competition, we must still conclude that there are at least two areas of economic activity where the market cannot be relied upon to allocate resources efficiently. The first of these is the well-known case of public goods. These are goods which must be consumed in equal amounts by all. Once produced, additional uses are costless. The most obvious kinds of public goods are such things as national defense, law enforcement and judiciary systems, flood control projects, free radio and television programs, etc. The price mechanism does not work in these cases because people who do not pay for the services cannot be excluded from the benefits that result. If these goods are to be provided at all, they must be provided from general governmental revenues with no direct user charges. I think

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[3] For further discussion, see for instance, P.N. Rosenstein-Rodan, "Programming in Theory and Italian Practice," in Max F. Millikan (ed.), *Investment Criteria and Economic Growth*, (Bombay : Asia Publishing House, 1961), pp. 17–32.

it is safe to say that, nowadays, even the most fanatical adherent of *laissez-faire* will admit that the government does have a role to play in the provision of public goods.[4]

The second area where the market is not likely, in itself, to lead to an efficient allocation of resources concerns the third assumption given above for the functioning of the classical model, namely, the assumption about special cases of increasing returns. The fact of the matter is that these special cases are not very "special" and cannot be ignored simply because they raise awkward theoretical problems. They constitute a large segment of the economic system which is crucial to economic growth and development. In theory, the rule of efficient allocation demands that producers must produce up to the point where marginal cost equals marginal revenue, which under perfect competition, is also equal to price. In situations of increasing returns, marginal costs are less than average costs. Hence, for the rule to hold, price must be below average cost, which means that producers will have to produce at a loss. Since it is accepted that businessmen are in business to make profits, and not for the sake of their health, it is clear that under such conditions these goods will not be provided by private enterprise. Let us take a very simple example as the limiting case. Suppose a private firm is considering building a toll bridge. Assume further that bridge crossing does not produce any wear and tear, and depreciation is solely a function of time and not usage. Under such conditions, the marginal cost of usage is equal to zero. By the efficiency criterion, price must also be equal to zero. No producer in this right mind would ever construct that bridge.[5]

Situations similar to the example cited arise in cases where fixed initial costs are very high relative to variable costs. A prime example of this situation is the case of public utilities and other social overhead capital. In the real world, the problem is not that private producers will stick to the rule of efficient allocation and thus refuse to produce at a loss. The real danger is that the investments involved are, as a rule, very substantial, and a few large producers capable of making such investments will tend to divide the market among themselves. They will then proceed to

[4] Strictly speaking, the examples cited belong to the category of social goods. Merit goods are another category whcih are rather different in concept. These are goods which are considered so meritorious that the government considers it necessary to interfere with individual and collective preferences. The most obvious examples of merit goods are education and public health. These services can be and are being provided by private enterprise, but if the government considers that society is not prepared to allocate sufficient resources, it then normally reserves to itself the right to intervene. (Negative cases of merit goods are such things as tobacco and liquor, where the government usually interfere with private preferences through taxation based on sumptuary laws).

It is important to distinguish the different bases for public intervention in the cases of social and merit goods. In the former, the government does not attempt to interfere with private preferences. It only seeks to provide services where the market fails to operate. In the latter case, the government consciously seeks to modify personal preferences. Consequently, there is less consensus on the justification for and the role of public intervention in the case of merit goods.

[5] Francis M. Bator, "Government and the Sovereign Consumer, " in Edmund S. Phelps (ed.), *Private Wants and Public Needs,* (revised ed.), (New York: W.W. Norton & Co., Inc., 1965), pp. 118–33.

produce in such a way as to maximize their monopolistic profits at very high prices. Thus a large segment of the consumers will tend to be excluded because of the high prices, resulting in a general reduction of collective welfare. And as social overhead capital is also a necessary ingredient of economic development, such practices can seriously retard the national development effort. These reasons explain why there is general agreement that in the field of public ulilities and other infrastructures, investment and operation are usually either undertaken directly by government or closely regulated by it. The discussion so far should also clarify the point that government intervention in these fields is not based on any illusion that it can operate an enterprise more efficiently than private business. It is not a question of efficiency, but of differences in objectives and motivation. In theory at least, private enterprise aims to maximize profit, while the objective of the public sector is to maximize collective welfare. Although actions in real life tend to depart from these "ideal" objectives, they are sufficiently clsoe for the rule to be taken as valid generally.

We have discussed two areas of activity where the market fails to function efficiently even under the assumption of perfect competition. It is now time to introduce more realism in our discussion by noting that there is much less than perfect competition in the real world. Dropping this basic assumption leads to some more serious difficulties. In real-world situations, the market mechanism works reasonably well in distributing consumer goods and allocating productive factors in the production process. There are several imperfections which are serious from the conceptual point of view, but practically, they are not significant enough to warrant large-scale public intervention. Where the market mechanism tends to break down is in the areas of allocating investment resources and of maintaining stability. Let us take a very quick look at these two problems.

There are three major reasons why the market tends to be inefficient in allocating investment resources. The first involves the whole question of externalities which had best be left until later because it is sufficiently important to deserve examination at some length. The second reason is the long life-time of capital goods which results in very serious problems of risk-taking under conditions of uncertainty. Having dropped the perfect–competition assumption, we can no longer pretend that anyone, including businessmen, has perfect information and foresight. Hence where risks are great, investment projects may not be undertaken even if there is clearly a great need for them. Long-term investments, such as large dams and reservoirs, railroad, or harbor construction are often as much a matter of faith as of rational economic calculation. The third difficulty stems from the indivisibility or lumpiness of capital. Certain kinds of investment, such as integrated steel mills, petroleum industries, and energy production can be made only in large chunks. The price mechanism does not work very well in such cases because it depends for its effectiveness on small rather than large changes. The difficulty is further compounded by the fact that these are also long-term investments, a fact which tends to increase considerably the risks to private investors.

On the question of stability, the classical model has little difficulty in demonstrating that, at any moment in time, the economic system will be in full equilibrium, given certain basic assumptions such as perfect knowledge and rationality, instantaneous adjustments, perfect liquidilty, and other institutional and behavioral conditions. There will be no maladjustment and all markets will be cleared automatically. Keynesian economics has shown that, even on theoretical grounds alone, this conclusion is not necessarily true. And in the real world where imperfect knowledge and adjustment lags play such a key role in economic activity, the conclusion is inevitable that there is no automatic mechanism for maintaining stability,in the sense of ensuring full employment of resources with price stability. This is an area where public intervention is generally accepted as necessary and, on the whole, beneficient.

Let us now turn to a brief consideration of the second necessary condition of the classical model, namely, that we disregard the ethical question of income distribution. In real life this question is too important to be ignored. In terms of economic growth and development, personal gains are probably the strongest and indispensable incentive for popular participation. And without popular participation, voluntary or otherwise, no society can really hope to achieve much in terms of economic and social development. Politically, glaring inequities in the distribution of income are very dangerous, especially in the context of present-day rising expectations. Enlightened self-interest dictates that the privileged classes should not impede efforts of the government to correct these inequities. In terms of social responsibility and ethical values, a strong case can also be made that the government has an obligation to see to it that all segments of the population have a reasonable share in the national wealth and income.

I have left the case of externalities and inter-dependence to the last because it is a major justification both for general governmental intervention and for development planning. Externalities are those portions of benefits or costs which are not absorbed by the units generating them. Interdependence denotes the concept that the satisfaction of consumers does not depend entirely on their own consumption, but partly on that of other consumers also. Economists used to struggle with the concept of external economies and diseconomies: they were sure it was very important but were hard put to come up with convincing examples. A widely-quoted bucolic example used to be the case of the benefit reaped by a bee-keeper from his neighbor's orchard. The difficulty was not cleared up until it was pointed out that there were basically two different kinds of externalities, one technological and one pecuniary.[6] We do not have time to go into details here, but the point is that externalities can be and usually are quite extensive. Let me just cite a few examples:

An industrial firm decides to locate a large processing plant near sources of raw materials in the hinterland of a developing country. In order to bring its outputs to a port city, it has to build a new highway. The highway will benefit the whole countryside but the firm will normally be unable to capture the whole of the benefit generated by its action.

[6] Tibor Schitovsky, "Two Concepts of External Economies" , *Journal of Political Economies*, Vol. LXII, No. 2 (April 1954), pp. 143–51.

The manager of a factory has to train skilled workers because there are very few of these in the area where he is located. Some of the workers may move to another firm after they are trained. The second firm benefits while the training costs, which may be considerable, are borne by the first company.

On the reverse side of the coin, we can also cite many cases of diseconomies external to the generating unit. An example would be the location of a slaughter house in the midst of a residential district near a kindergarten. The slaughter house may create traffic jams, health harzards, nuisances, and endanger the lives of small children. These are very real social costs but they are borne by people in the community and not by the owner of the slaughter house.

A large mining company dredges extensively for minerals, say tin and wolfram. In the process, thousands of acres of land are rendered worthless for any other uses. The company reaps the profit while society bears the costs.

It is not only well-to-do businessmen who may create external diseconomies. Even the poorest subsistent farmers can be equally costly to society. Take the case of slash-and-burn practice in farming. If a large enough number of farmers uses this method of cultivation, a whole region may be changed from a potentially fertile farm land to an arid desert.

We can go on at great length about the problem of the divergence between social and private gains or costs, but the few examples given above should suffice to show that the problem is a real and serious one. This problem is sometimes referred to among planners as the "neighborhood effect" and it serves as a strong justification for the government to intervence in order to correct any misallocation of resources that may occur through the operation of the free market. In the case of the consumer, the concept of interdependence points to the fact that consumption in absolute terms is not a very meaningful indication of satisfaction or welfare. It does not make much sense to hold that people of a certain class, say the worker, should be more satisfied because their real income has increased if, at the same time, the income of other classes has risen much more. People tend to compare their income and consumption with those of others, especially those of higher-income classes. The point of this discussion is that it tends to support our previous arguments about the need for correcting inequities in income distribution.

Let us pause here to recapitualate the discussion and summarize the arguments presented so far. According to our arguments, the six areas of activity where there are serious limitations to the market mechanism are:

1) Allocation of investment resources.
2) Maintenance of stability.
3) Distribution of income.
4) Provision of public utilities and other social overhead capital.

5) Allocation of resources when there is serious divergency between social and private gains or costs.

6) Provision of public goods.

The role of government in economic affairs follow almost automatically from the above discussion. Generally speaking, it is in these six areas where public intervention is greatest.

Before going on to a discussion of the role of government, however, let us first consider briefly the benefits that the private sector can derive from public intervention. I think we can identify at least five major benefits in this respect. First, consider the case of public provision of social overhead capital. The so-called "hard" SOC includes such things as highways, railroads, harbor installations and facilities, power plants, water supply, and communications installations, while the "soft" SOC includes education, public health, and technical training facilities and services. An increase in the public provision of these infrastructures is likely to lead to substantial reductions in production costs. It may also, as in the case of manpower training, make it easier to achive a more efficient management and administration of various enterprises. A second benefit to accrue to the private sector is that the government, by supporting certain measures of a risk-hedging nature, may make it easier and more profitable for business to invest in high-risk ventures. (A prime example of this is governmental guarantee of mortagages for the hire-purchase of private dwellings). Thirdly, by maintaining stability, the government can contribute greatly to business prosperity and security through the prevention of violent business cycles.

The benefits outlined above tend to accrue directly to business, but there are others which, while less direct, are by no means unimportant. The provision of public goods, such as national defense and law enforcement are equally necessary to the business community as to other segments of society. Public provision of merit goods such as education and public health are less important to businessmen because they tend to make use of expensive private facilities and services. But even here, enlightened self-interest indicates that it is dangerous for the privileged classes to exist as islands of sanity in a sea of darkness and ignorance. In a wider perspective, a higher level of collective welfare is likely to lead to higher personal welfare because of the greater availability of amenities. I have concentrated on the question of self-interest not because businesemen are more selfish than others, but because, as I have pointed out earlier, self - interest is a prime motivation of action and an indispensable basis for cooperation. We shall leave the question of what government can and should do specifically to aid business in order to achieve more rapid development until later when we come to discuss development planning.

II. The Role of Government

Following from the above discussion on the need for public intervention, we can identify four major roles of government in economic affairs. These are:

1) Correction of misallocation of resources, due to externalities, improper investments because of risks and imperfect knowledge, and the need for public goods and social overhead capital. The purchases of goods and services for this purpose constitute major portion of total governmental purchases.

2) Adjustment in income distribution. The main mechanism here is transfer payments, that is, payments without services rendered. Another policy instrument is public investments. By choosing certain kinds of investment projects, the government can help to increase the income of selected occupation groups, such as farmers, by increasing productivity, reducing costs of production and transportation, and stimulating market demand. Such actions can, obviously, have significant impact on the pattern and rate of growth and development.

3) Maintenance of stability, in the sense of maintaining full employment of resources together with a stable value of money. The major mechanisms of intervention in this case are fiscal and monetary instruments and public investment policy. For instance, if there are serious deflationary pressures, the government may decide to reduce taxes and increase transfer payments, leading to an increase in disposable income. It may also choose to increase public investment. Such action would tend to lead to an increase in aggregate demand and bring the economy back to a full-employment equilibrium. On the other hand, under inflationary conditions, the government may reverse these actions in order to retard the rate of increases in aggregate demand. Monetary policies can also be very useful in influencing the levels of consumption and investment.

4) Guidance of economic growth and development. In developed countries, the problem is one of maintaining a "satisfactory" rate of growth with full employment and price stability. In developing countries, it is more a matter of attaining a more rapid rate of development commensurate with other requirements. This function has now become one of the most important responsibilities of governments in developing countries.

We shall concentrate on the fourth function, namely, the acceleration of growth and development. The first point to consider in this regards is that there are two interrelated but distinct aspects of the question of resource allocation for development. These are a) resource mobilization and, b) resource utilization. In terms of resource mobilization, the government is clearly in a unique position to assemble the resources necessary for development through its taxing power, usage of various instruments of guidance and control, and its position to obtain assistance from external sources, especially in terms of capital inputs and technical know-how. The situation is quite different in the case of resource utilization. There is no intrinsic reason why public officials should be more efficient than private enterpreneurs inthe use of resources. Usually it is the other way round. Lacking the powerful motive of private profit, public officials, even under the best circumstances, tend to be somewhat careless about how scarce resources are used. And given the prevalent lack of motivation, efficiency, and one might say, honesty, among government officials in most developing countries, I think it would be fair to conclude that public officials should be kept away from direct management of enterprises unless there are clear indications. that they would be more efficient than private enterpreneurs in exceptional circumstances.

Another distinction which should be borne in mind is the difference between public provision and public ownership and management. The fact that certain goods or services are to be provided by the public sector by no means implies that the government must own or manage the enterprises producing these goods or services. Let us examine two extreme examples concerning public goods. In the first case, all goods are produced directly by the public sector and then sold to consumers. The government owns and manages all productive enterprises but there is absolutely no provision of public goods. At the other extreme, all goods are produced by private enterprise and then sold to the government. The government purchases these goods from its general revenues and then distribute them free of charge to consumers. In this case, all goods are provided by the government, but there is no public ownership or management.[7]

Hence a general rule which should be applied in the division of labor between government and private enterprise is simply this: Who can do it better? The government should only step in where private enterprise cannot do it or where it is clear that the government can do it more efficiently. There is, for instance, no reason why government should not mobilize resources and make them available, with proper and adequate safeguards, to the private sector where the latter is capable of utilizing them more efficiently. Examples of this include the establishment of such institutions as investment banks, agricultural development banks, industrial finance corporations, and agencies to assist in the financing of small businesses. But please note that in judging relative efficiency between the two sectors, the criterion to be applied is public rather than private benefits.

III. Development Planning

We shall continue to examine the question of the role of government in accelerating economic growth and development by taking a quick look at development planning. It is not the place here to discuss planning theory and its various ramifications.[8] Let me simply point out that the two key elements of planning are choice and control.[9] The first denotes a process of

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7 Richard A. Musgrave, *The Theory of Public Finance* (New York: McGraw-Hill Book Co., Inc., 1959), p. 15.

8 For some useful discussion of these matters, see for instance: Herbert A. Simon, *The New Science of Management Decision* (New York: Harper & Brothers Publishers, 1960); John W. Dyckman, "Planning and Decision Theory," *Journal of the American Institute of Planners*, Vol. XXVII, No. 4 (November 1961), pp. 335-45; P. Davidoff and T.A. Reiner, "A Choice Theory of Planning," *Journal of the American Institute of Planners*, Vol. XXVIII, No. 2 (May 1962), pp. 103–15; Thomas A. Reiner, "Sub - national and National Planning: Decision Criteria," *Papers of the Regional Science Association*, Vol. XIV (1965), pp. 107–36.

9 For further discussion, see: Edward S. Mason, *Economic Planning in Underdeveloped Areas: Government and Business* (New York: Fordham University Press, 1958), ch.III.

selecting the most appropriate course of action out of a set of possible alternative actions, while the second refers to the exercise of authority and influence in order to implement plan provisions. In this view, planning without implementation is no planning at all; it is merely an academic exercise which is not likely to be of much benefit to anybody.

Since the end of the Second War, a great number of developing countries has adopted development planning as an instrument for accelerating economic and social development. Unfortunately, there has been such a diversity of activities subsumed under development planning that the term has ceased to be very meaningful. For our purpose we may say simply that, in mixed economies,[10] that is, in economies where both the public and private sectors are important, development planning is:

> *a systematic process to guide and influence the development process by supplementing, reinforcing, supporting, and guiding the market process.*

The important point to note here is that planning and the market are not mutually exclusive. They are in fact complementary, in the sense that planning only tries to help where the market does not work very well. It is, of course, true that planning inevitably implies some interference with the free play of the market, but judiciously applied, it can be a powerful tool to remedy the more serious weaknesses of the market mechanism. The end result is likely to be beneficient to private enterprise as well as to society as a whole.[11]

In order to see more clearly the benefits that can result from development planning, we shall have to consider very briefly what a development plan is. In the simplest term, a development plan is nothing more or less than a development strategy. Of course the contents, quality, and scope of individual plans can and do vary widely. To my mind, there are four elements which are essential to a good development plan. These are:

1) a rational program of public investment,
2) reasonable and adequate private-sector planning,
3) appropriate instruments of guidance and control, and,
4) adequate provisions for implementation.

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[10] A recent and useful examination of planning experiences in both mixed and centrally planned economies will be found in: United Nations, Department of Economic and Social Affairs, *Planning for Economic Development*, Vol. II, *Studies of National Planning Experience*, Pts. I and II, (New York: United Nations, 1965).

[11] For further discussion of the question of planning in mixed economies, see for instance: Gerhard Colm and Theodore Geiger, "Country Programming as a Guide to Development," in The Brookings Institution, *Development of the Emerging Countries: An Agenda for Research* (Washington, D.C.: The Brookings Institution, 1962), ch. II; Robert Shone, "Problems of Planning for Economic Growth in a Mixed Economy," *The Economic Journal*, Vol. LXXV, No. 297 (March 1965), pp. 1–19.

We shall only deal with the first, third, and fourth elements in passing. The second element, namely, private-sector planning will be discussed in more details because it is the one which concerns us most directly here.

As we have seen, investment is one of the functions which are not very well coordinated by the market mechanism. There is also a great and urgent need in developing countries for public utilities and other social overhead capital, such as highways, irrigation systems, communication facilities, water and sanitary services, education, public health, and a host of other requirements. Given the general lack of capital and the inadequacies of the market, the government is about the only unit in the economic system which can invest in such infrastructure. It is therefore crucial that the public development investment program be made as rational and expeditious as possible.[12]

Let us now turn to the second element of a development plan mentioned above. An important part of private-sector planning is what is generally referred to as indicative planning. This is a rather loose term referring to those parts of the plan where the aim is not the direction of public expenditures or the control of private activities, but rather the guidance of private-sector operations towards desired ends. Since we are concerned mainly with the private sector here, it will be necessary to examine this element in somewhat more details. Plan targets for the public sector are controlling but not mandatory. They control public development expenditures but do not authorize actual disbursement. Authorization can only come through the budgettary process. Targets in the private sectors are not even controlling; they serve only as a guideline for private enterprise. In developing countries there are usually very few corporations large enough to undertake the extensive short-term forecasting and long-term projections necessary for accurate and satisfactory planning of enterprises. Planned targets in both the public and private sectors, if well constructed, can serve as a very useful indication of what business can expect during the time period of the plan. They can also help business to be more aware of government policies and intentions which may have significant repercussions on private operations. Another factor which should be borne in mind is that what a private firm should do does not depend only on its own activities but also, and to a large extent, on what other firms intend to do. This is true because of the linkages among firms in an industry and among industries and the various sectors in the economy. By predicting the future structure and interrelationships, a well-conceived plan may greatly help businessmen to perceive opportunities which may otherwise be missed, and conversely, to avoid mistakes which are likely to be made without the information provided by the plan.

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[12] For a recent discussion of the need for rational planning of the public sector, see: W. Arthur Lewis, "Planning Public Expenditure," in Max F. Millikan (ed.), *National Economic Planning* (New York: Columbia University Press, 1967), pp. 201–29..

Let us now consider what the government can and should do to assist private enterprise through its planning instruments. Major elements of private - sector planning include the following:[13]

1) Provision of information on development potentials. The information should be based on surveys and careful analysis including:

a) resource surveys,
b) research on better methods of resource utilization,
c) market surveys, analyses, and forecasting, and,
d) estimation of overall trends of future development.

2) Assistance in the creation of more and better markets. This assistance should include the protection and improvement of competitive positions in international markets.

3) Granting of promotional privileges which should be of considerable benefit to new ventures. On the other hand, it should be noted that the government should also be free to impose penalities in order to discourage activities which are clearly harmful to the development effort.

4) Provision of adequate social overhead capital.

5) Improvement of the legal framework, especially by removing unduly restrictive legislations and legal practices.

6) Promotion of increased saving, both private and public, as well as assistance in obtaining capital from external sources.

7) Effectuation of administrative reform leading to greater efficiency and honesty in governmental activity and greater convenience for private enterprises in their dealing with the bureaucracy.

We shall only comment in passing about the remaining elements of what I consider to be a good plan. Appropriate and adequate instruments of control and guidance are indispensable to the success of a plan. Without these, plan objectives tend to be not much more meaningful than pious hopes and the specification of targets becomes merely an academic exercise. This does not mean that the plan document should spell out in every detail the manner in which the government intends to persue its planned objectives. It would be politically inexpedient to do so, because governments prefer to leave sufficient room for political manuevering. What it does mean is that policy instruments for plan implementation must be carefully worked out, but they need not be published for public consumption. The plan document itself should, however, contains sufficient information on policy instruments to provide a broad outline of government policies in the various

[13] See also: W. Arthur Lewis , *Development Planning: The Essentials of Economic Policy* (London : George Allen & Unwin, Ltd., 1966), ch. I.

areas covered by the plan. As for the fourth element, namely implementation, it is largely a question of organization and administrative procedure. Inappropriate organization and inefficient administration together constitute one of the greatest obstacles to plan implementation in particular and the effort to accelerate development in general. We shall not go into details here. Suffice it to say that without adequate provisions for implementation, a plan is not much more than a decorative document.

To sum up, we may say that development planning, as a tool for accelerating growth and development, should be directed mainly towards three areas of activities. These are:

1) Public investment, to provide public goods, public utilities, and social overhead capital needed for economic and social development.

2) Public enterprises which should be confined strictly to large-scale and/or high-risk ventures where private enterprise cannot, for one reason or another, undertake and operate effectively.

3) Promotion and encouragement of the private sector through the various means discussed above.

It follows from the above arguments that development planning can be of great value to society as well as to private enterprise. However, it would be a grave mistake to claim too much for development planning. As an instrument for development, it attempts to serve and harmonize various and divergent requirements and objectives. In a nutshell, I think it would be correct to say that the basic problem of development planning is:

> *How to acheive a satisfactory rate of growth while maintaining a high level of employment, price stability, and a "proper" state of income distribution, within the constraints set by political and socio-cultural requirements.*

It is obvious that these can be, and usually are, conflicting goals and objectives. The resolution of these conflicts are political rather than economics in nature. The economics of planning is thus one of second or third, or even fourth, best rather than one of optimization.[14] In the last analysis, the efficacy of planning depends much more on the good judgement, and one might say, the wisdom of government leaders and administrators than on the technical proficiency of planners. Planning cannot be a substitute for good judgement and wisdom, and without these, it can actually be harmful rather than beneficial to national development. However, properly used, it can be a powerful tool for raising developing nations from their present levels of poverty and backwardness.

IV. The Role of Business

We have spent some time on the question of what government can and should do in the common effort to accelerate national development. It now remains for us to see what business

[14] Mason (1958), *op.cit.*, p. 66.

can do. Being ignorant about actual business operations, I feel a terrible qualm in trying to beard the lion in its den. Furthermore, it is a wellknown fact that the outstanding ability and efficiency of Hong Kong businessmen as well as their high standard of integrity are an envy to all her neighbors. It is, therefore, quite likely that a great deal of what I shall have to say would be inapplicable to the local situation. So let us just say that I shall be speaking in a general sense and mainly from the point of view of an ignorant, but highly sympathetic, civil servant. The first point I should like to raise is not at all controversial. It is this: that private enterprise can do a great deal in helping the common cause simply by improving it own internal efficiency. Increased efficiency in production and management will not only result in cheaper and better products, but also in improving the competitive position of the country in international markets. This would, in turn, lead to higher income, greater effective demand, and more output. The end result is likely to be that the rate of growth will be substantially increased. I shall leave the question of enterprise management to the experts who, I am sure, will discuss this mater exhaustively in other sessions of this seminar. Let me simply remark in passing that the application of managerial economics and modern decision theory can be of considerable value in this respect. A related aspect of this problem is the question of business ethics. Dishonest practices and underhand business methods can be very discouraging to potential investors, both local and foreign. They can also be ruinous to the trading position of a country in the long run. These facts are self-evident, but it is regrettable that some businessmen in developing countries tend to indulge in sharp practices with no regard for the harmful effects on the business community and the country as a whole. In any occupation, there will inevitably be some black sheep, and the business community should adopt adequate measures to police itself. If businessmen do not do this themselves, then someone else will eventually do it for them, in which case the result is likely to be far more painful.

Another area where business can be most helpful to the national effort is in the field of innovation. Unfettered by antiquated regulations and bureaucratic red tape, private enterprise is, or at least should be, in a much better position than government to initiate changes. I would even go so far as to say that business has an obligation to society to act as an agent of change because it is in the most favorable position to do so. It can always be argued that businessmen in developing countries tend to stick to the beaten track, not because they are innately conservative or unimaginative, but simply because the risks involved are too high. There is some truth in this argument, but it may not be the whole truth. It would be tragic if we could induce the government to adopt risk-reducing measures only to find that the private sector is not responsive because it thinks it is doing "well enough". Let us not forget that economic and social development is a joint responsibility of all segments of society. If the basic role of government is to mobilize resources, then it is largely up to business to make the best use of those resources. In other words, my contention is simply this: that in developing countries, the businessman should act more as an enterpreneur and less as a corporate administrator or bureaucrat.

The third field of activity where business can be very useful lies in assisting the government in the provision of merit goods, especially education and public health. The burden of providing adequate educational and health services is becoming extremely heavy for governments partly because of rapid population growth and partly due to higher standards expected. If a part of business earnings is set aside to support foundations and other non-profit organizations to provide such services, the business community can play a fruitful and worthwhile role in national development. For in the long run, the single most important factor in development is probably the quality of the human resources. It is true that business is already assisting the government to a limited extent in this field. My point is that a great deal more can probably be done if an active cooperation can be established between government and business.

This discussion leads to my fourth and final point which concerns the cooperation between the public and private sectors. I should like to advance the notion that business should, for the sake of collective welfare, willingly cooperate with the government even against its own interest in cases where it is clear that public gains would outweigh private losses. This is an ethical rather than an economic question, and I do not want to insist on it because it depends to a great extent on individual value judgement. Let me just point out that a certain amount of self-abnegation and altruism is likely to be beneficial to all concerned in the long-, if not in the short-run.

In conclusion, I would like to say that if the above arguments are conceded, then there would appear to be a wide area where cooperation between government and business is both possible and fruitful. On the side of the government, a great deal can and should be done to assist and encourage the private sector in its various operations. This can be done indirectly through the judicious use of appropriate policy instruments, or more formally through development planning. On the reverse side of the coin, business also has certain functions and obligations to perform in the common effort to accelerate economic and social development. With good will and perseverance, I am confident that such cooperation is possible. In this respect, a better understanding among government officials and businessmen of the complementary roles of the two sectors will help greatly in improving joint effort and cooperation. If my talk today succeeds in contributing to this understanding, however slightly, I shall be more than satisfied.