Strategic Policy Intervention

- Washington Consensus (IMF, WB, WTO): policy agenda of late 1980s-1990s
  - Return to mkt-based development (mkt mechanisms)
    - Remove price controls
    - Liberalize trade; X-led growth of non-traditional exports
  - Structural reforms and re-regulation:
    - Privatization, property rights and ↑ private sector's role
    - Foreign participation to ↑ investment
    - Ease of doing business: simplify regulations to ↑ competition
  - Sound fiscal and monetary policy
    - Limit budget deficits; prioritize G on health, ed, infrastructure
    - Broaden tax base, reduce subsidies
    - Central bank independence: control inflation and mkt-based interest
    - More flexible exchange rates; rates that help export-led growth

Strategic Policy Intervention

8.2 East Asian miracle: What was the strategy and what was trade policy's role?

- Fast economic growth through
  - Market-based economies, but
  - Strategy of state intervention (not state planning)
    - Support infant industries
    - Promote exports (not export subsidy)
    - Mobilize savings and investment
- Comparison of E. Asia and Latin America

Strategic Policy Intervention

- Trade policy's role: Asia's miracle vs Latin America's ISI

	Asian experience	**LA experience**
% Δ GDP	1960-90s: Tigers @ 8-9% 1980-2010: China @ 10%	1960-1980: BZ at +5% 1980-2010: BZ at 3%; only Chile had 7%
Trade policy regime:	+ BOT (balance of trade)	- BOT until after 2000
Export regime	X-led: ↑ X as % GDP; export-led ISI X as %GDP > 100%; diversified X	↓ trade as % GDP BZ: lower trade as %GDP than developed
Import regime	Avg protection at 24%; More trade-openness; Managed trade: X-targets and trade-balancing requirements Low protection level of intermediate inputs	Avg protection at 46% Some sectors: PSE > 200% Reflects inward-orient ISI More restrictive of intermediate inputs because of BOT problems
Industrial and Macro Policy (Y = C+I+G): saving, investment, K-inflow, FP (G), MP (E)		
Consume, saving and investment policy	C low; aggressive saving, I policy; China: dom savings +40%; I/GDP = 50% (90% goes to SOEs who acct for ⅓ of GDP)	C high (60% of GDP); low save (< 20% of GDP); High dom + foreign debt; BZ: I (19% of GDP); FDI less welcome (nationalization)
K-inflows	High saving, I + foreign debt less problematic; FDI with conditions	Low savings → ↑ K-inflow esp if ISI is K-int; foreign currency loans → risk of BOP crises
MP and FP	$G < T$; MP to fix currency value	$G > T$; debt is monetized; foreign debt
Exchange rate	Undervalued currency → ↑ X	Overvalued + devaluation of local currency

Strategic Policy Intervention

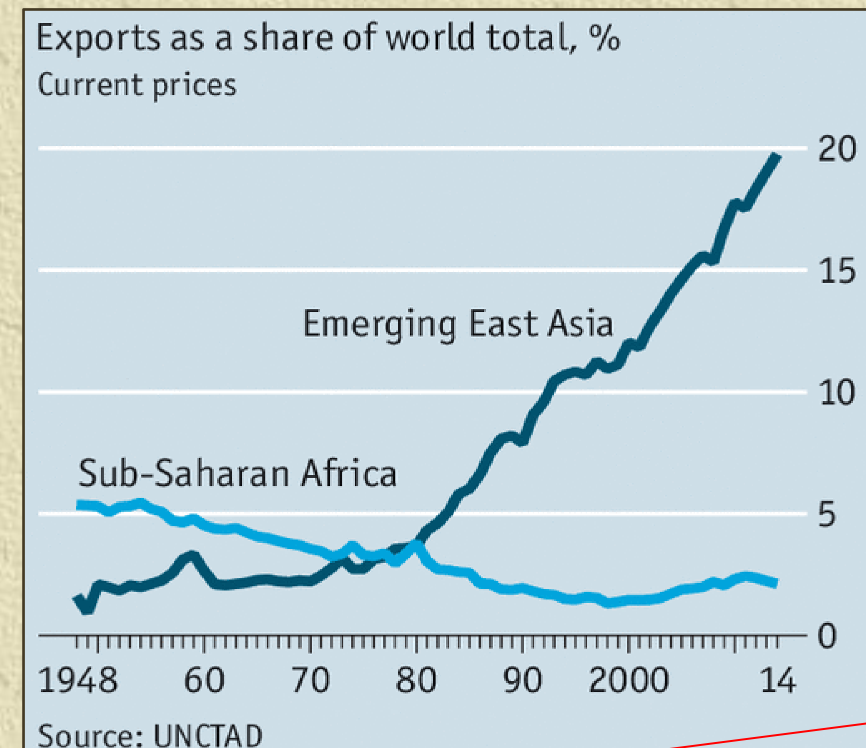
- Trade as % GDP, (X+M)/GDP in %

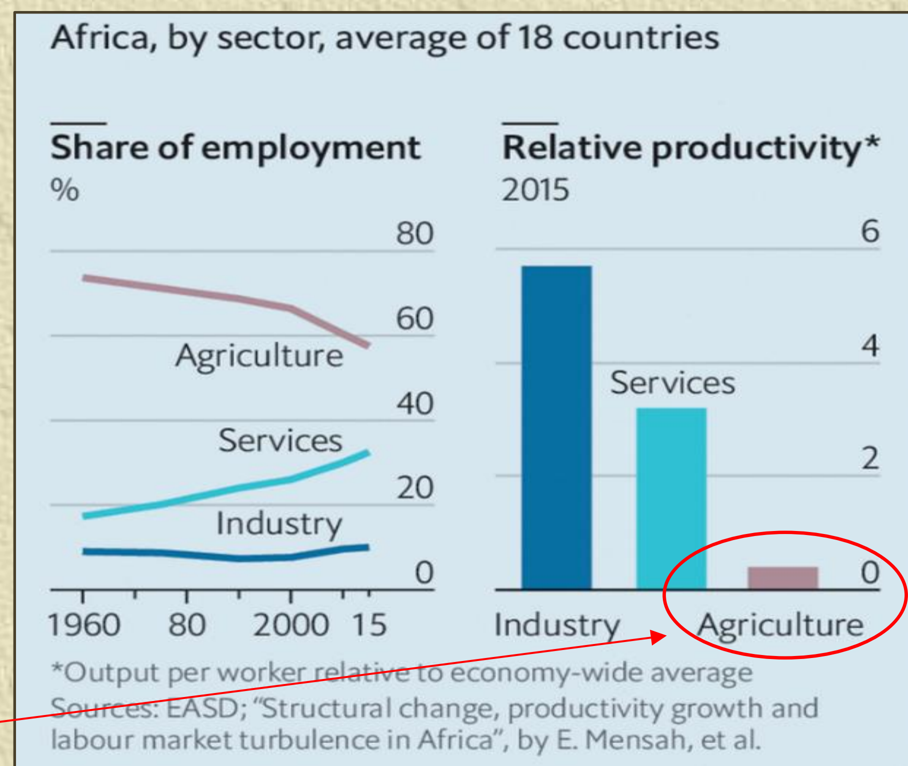
Asia				Latin America		
	1960	2016			1960	2016
Indonesia	24	37		Argentina	15	26
Malaysia	113	128		Brazil	14	25
Korea	15	78		Colombia	30	35
Japan	21	15		Chile	29	56
Vietnam	-	185		Mexico	20	78
Singapore	339	318		Peru	40	45
Hong Kong	-	373		LA & Carib. Avg	22	43

Source: World Bank, 2017, https://data.worldbank.org/indicator/NE.TRD.GNFS.ZS

Strategic Policy Intervention

- Export-led vs inward-oriented growth: Asia vs Africa





Ag productivity: Africa has about ½ the world's uncultivated arable land. Erratic rainfall means it must switch to drought-tolerant varieties or plants to mitigate the problem. 50 yrs ago Africa was one of the world's great crop-exporters. Ghana grew most of the cocoa, Nigeria was biggest exporter of palm oil and peanuts and Africa grew ¼ of all coffee.

Economist, "Industrialisation in Africa: More marathon than sprint", 07 Nov 2015; "Agriculture in Africa: Wake up and sell more coffee", 19 Sep 2015, p. 33-4; "Industry in Africa: Will it bloom?", 13 Jan 2020, p. 23-4.

Strategic Policy Intervention

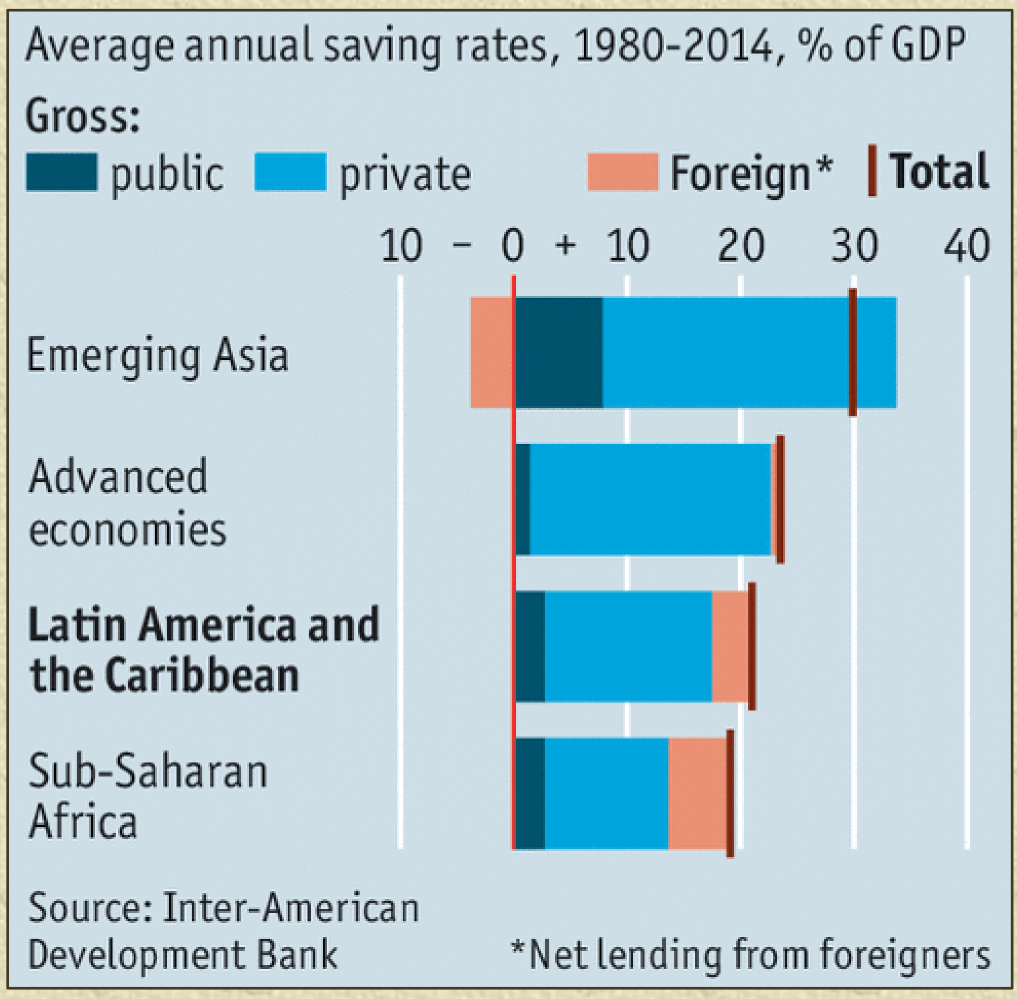
- Latin America's continued dependence on revenue from resources

Latin America remains dependent on commodities for growth. Between 2000-10, it accounted for 52% of region's export, down from 86% in the 1970s. E. Asia fell from 94% to 30% over same period.

Source: *Economist,* "It's only natural", Special report on Latin America, 11 Sep 2010, p. 5.

Strategic Policy Intervention

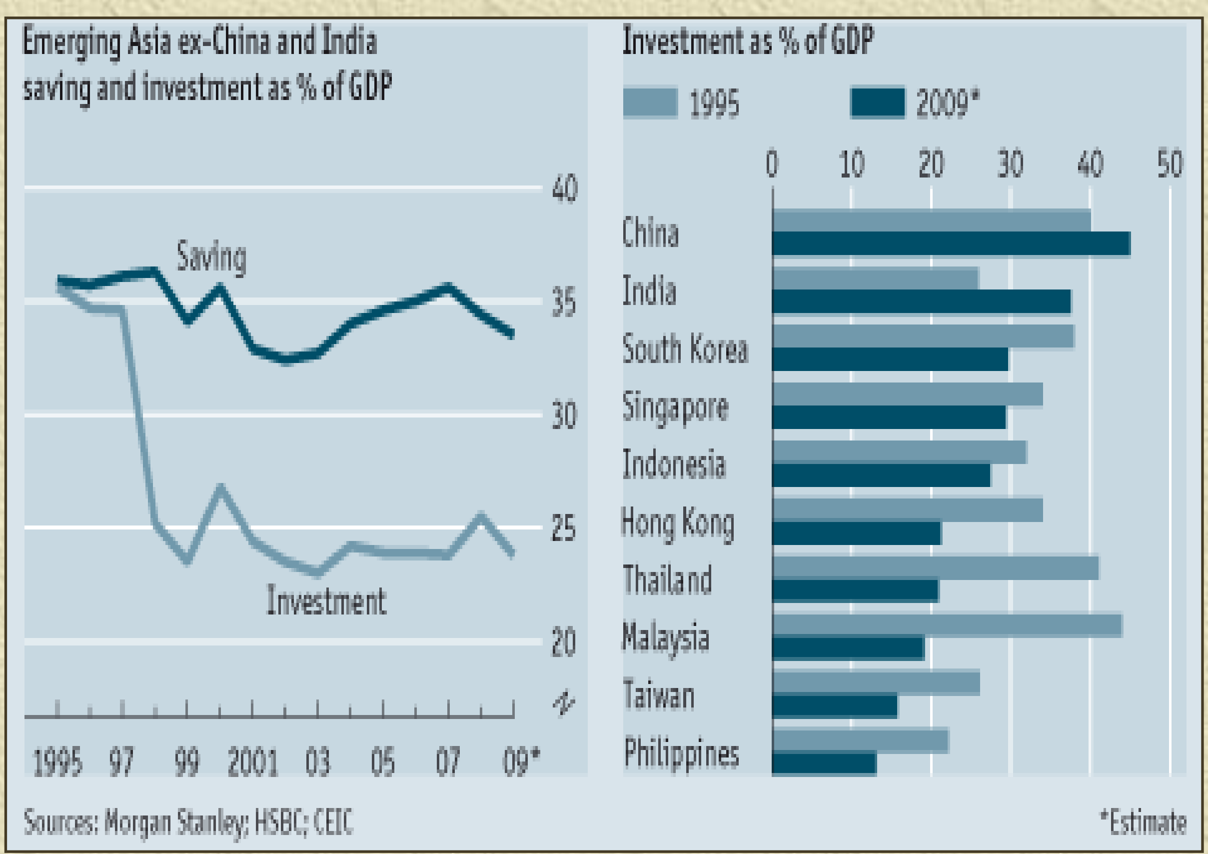
- Importance of savings
  - Low LA savings rate
    - Foreign K is not perfect substitute for local savings
    - Foreign K is mobile and leaves when it is most needed
    - K-inflows raise currency value hurting export sectors
  - For 5% GDP growth, need I of about 25% of GDP
    - Some countries reached this during commodity super-cycle of 2003-13
  - Weak financial systems
    - Bank loans to private sector is 30% of GDP (80-100% in DCs)
  - G > tax, too little spending toward I in infrastructure



Economist, "Bello: Those spendthrift Latins", 2 Jul 2016, p. 47.

Strategic Policy Intervention

- Saving, investment and consumption in emerging Asia/China



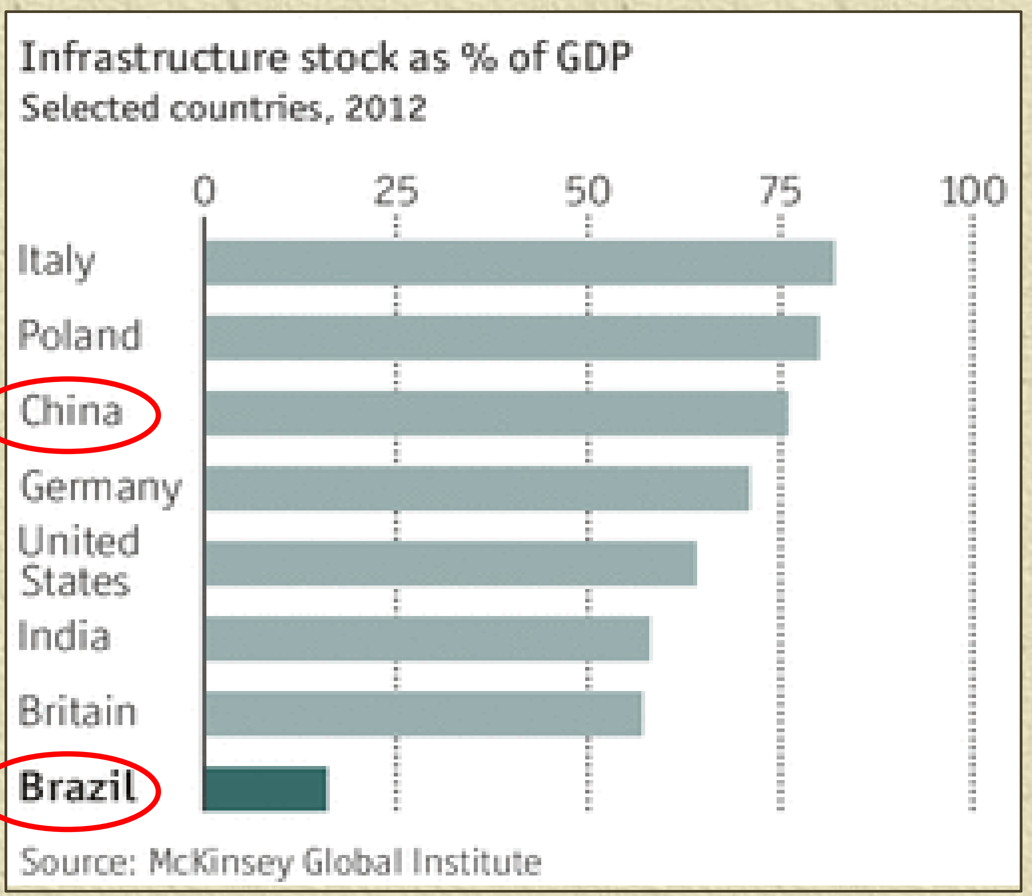
Economist, "Economics focus: Invested interests", 23 Jan 2010

Economist, "Free exchange: A reasonable supply", 30 Nov 2013

China's K-accumulation of imported physical K was financed by domestic savings. ↑K-intensity of the growth model in M-prodn and infrastructure investment meant high savings and low C/GDP. Heavy reliance of export.

Strategic Policy Intervention

- Investment in infrastructure



Brazil’s infrastructure is decrepit, ranked 114 out of 148 countries. Just 1.5% of Brazil’s GDP goes on infrastructure investment from all sources, public and private. Total value of Brazil’s infrastructure is 16% of GDP where other large economies avg 71%.

Economist, “Infrastructure: The road to hell”, special report, Brazil, 28 Sep 2013, p. 9-10

Strategic Policy Intervention

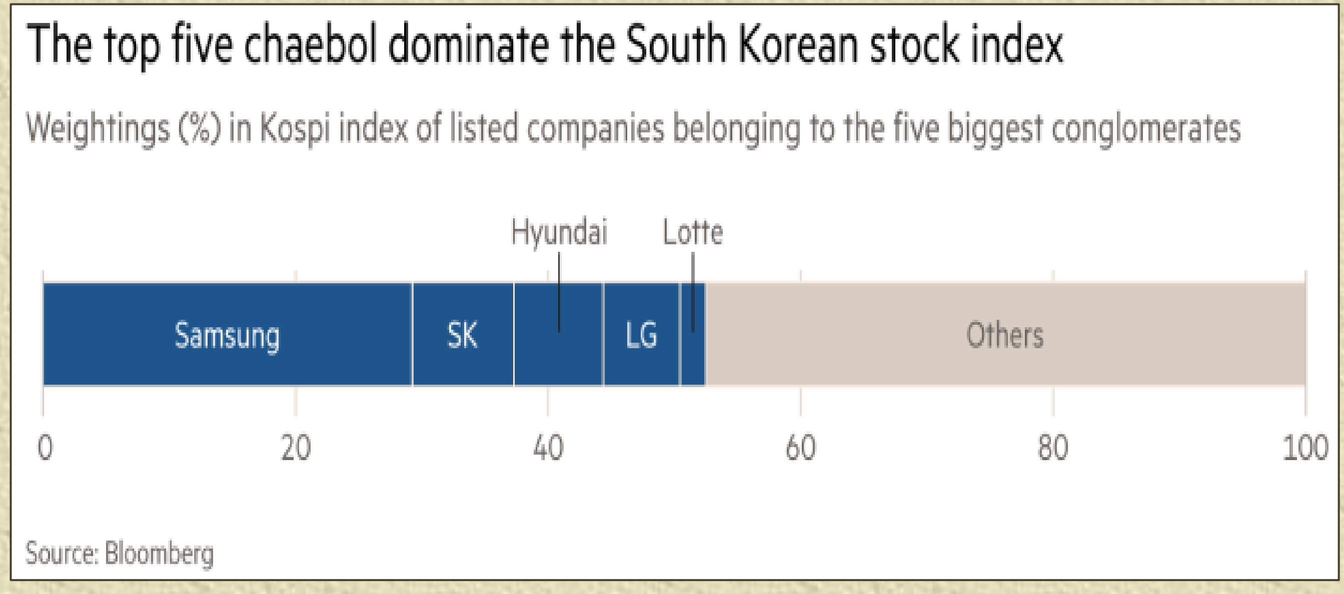
- Asian miracle vs Krugman's thesis
  - Trade openness
  - Capital accumulation
  - Total factor productivity

- Asian financial crisis 1997: problem with the strategy
  - Economic case against X-led growth at all cost
    - Macro imbalances
    - TOT implications
    - Over-investment

Economist, "Bello: Latin America's Korean dream", 20 Sep 2014

Strategic Policy Intervention

- Political argument: case of South Korea
  - Chaebol (corporate conglomerates)
    - 10 main *chaebol* account for > 70% of profits of all listed firms
    - 4 chaebol acct for 47% of output; 50% of exports and 20% of employ
  - Samsung's sales = 20% of GDP (shipbuilding, life insurance, smart phone)
  - Second-tier chaebols survived 2007 financial crisis through state support

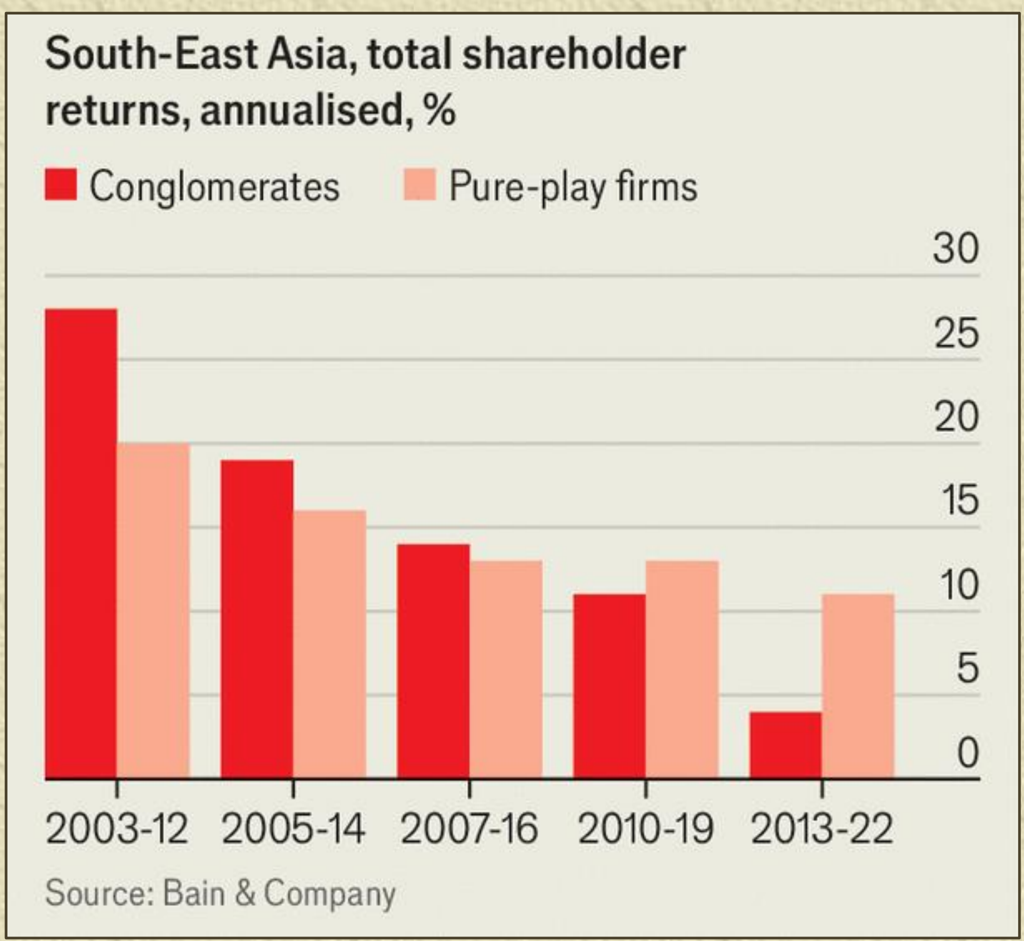


Samsung's rise mirrors S. Korea's. Its influence led to 2 bribery convictions, including of the president - and twice pardoned as the firm is seen as being in the national interest

Economist, "S. Korea's Economy: What do you do when you reach the top?", 12 Nov 2011; "Chaebol failures spark sharp rise in bad loans", *Fin Times*, 14 Oct 2013, p. 18; "Samsung: Losing its shine", *Economist*, 9 Feb 2008; *FT*, "In the shadow of a giant", B. Harris, 20 Aug 2018, p. 7.

Strategic Policy Intervention

- SE Asia's conglomerates slowing mkt dynamism



Among top 50 firms in SE Asia by revenue, only one, a gaming and e-commerce firm from Singapore, was founded since 2000. SOEs account for 15 of top 50. Subsidiaries of conglomerates (ag, energy, property, banking, etc.) account for another 14.

Extensive political ties dampen the incentive to innovate. Foreign-ownership restrictions shield them from competition. Cosy relationships with regulators keep domestic upstarts at bay, too.

Note: a pure-play firm is one that is publicly traded focusing its efforts and resources on only one line of business or industry.

Economist, "Business in Asia: Tropical depression", 26 Oct 2024, p. 55-6.

Strategic Policy Intervention

- Crony capitalism

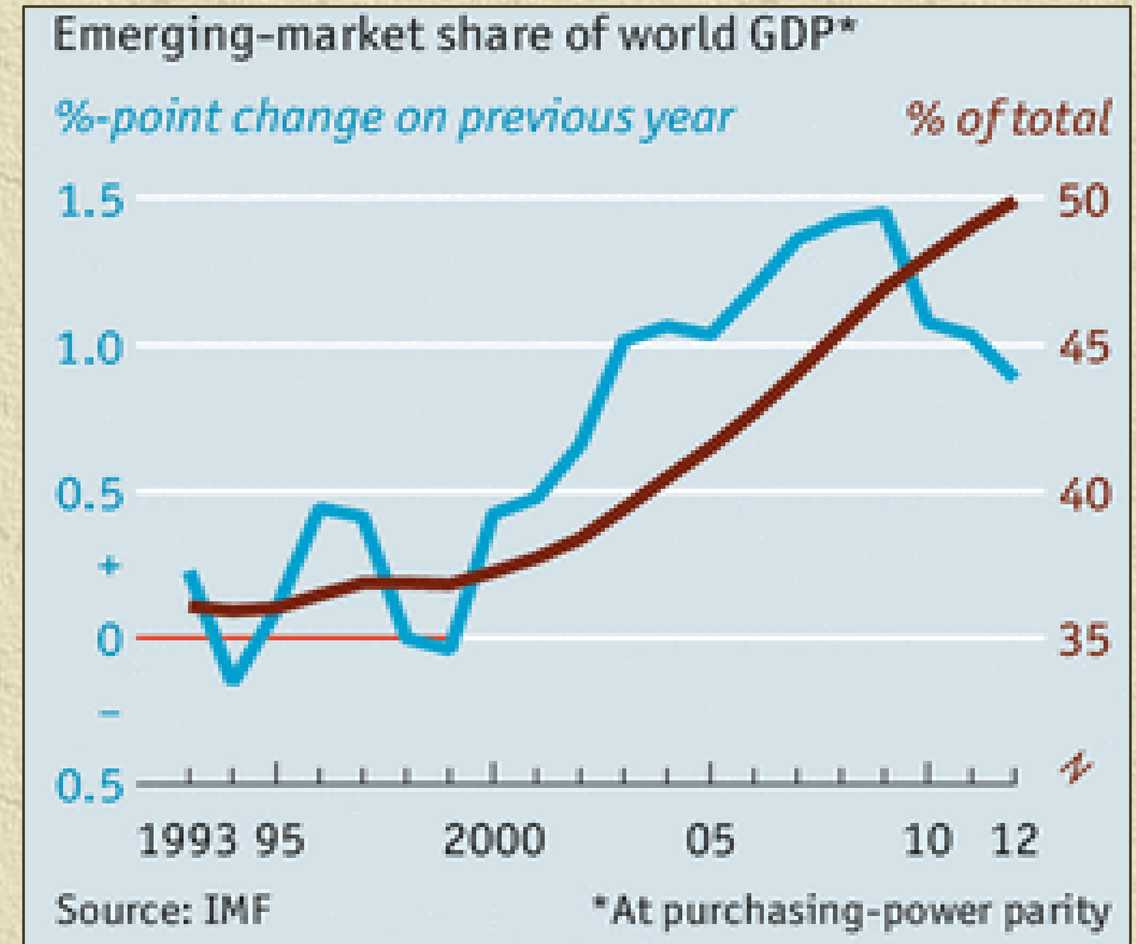
All of the BRICS (Brazil, Russia, India, China and S, Africa) emerging economies are ranked among the highest on the index. They are joined by mostly E. Asian economies.

The index considers billionaires whose wealth is deemed to be from "rent-heavy" sectors, but it does not measure actual relationships between agents and gov't.

Economist, "Our crony-capitalism index: The party winds down" 7 May 2016, p. 10-11. see also limitations of the index: https://globalanticorruptionblog.com/2014/03/31/the-economists-crony-capitalism-index-does-not-measure-crony-capitalism/

Strategic Policy Intervention

- Catch-up growth, middle income trap, de-industrialization
  - Is "catching up" slowing down?



Industrialization is how North got rich. LDCs can grow fast by copying, importing K and learning rich world's know-how. Once cheap L_A shifts to M-sector, wages ↑ and K/L ratio ≈ rich country level - growth slows.

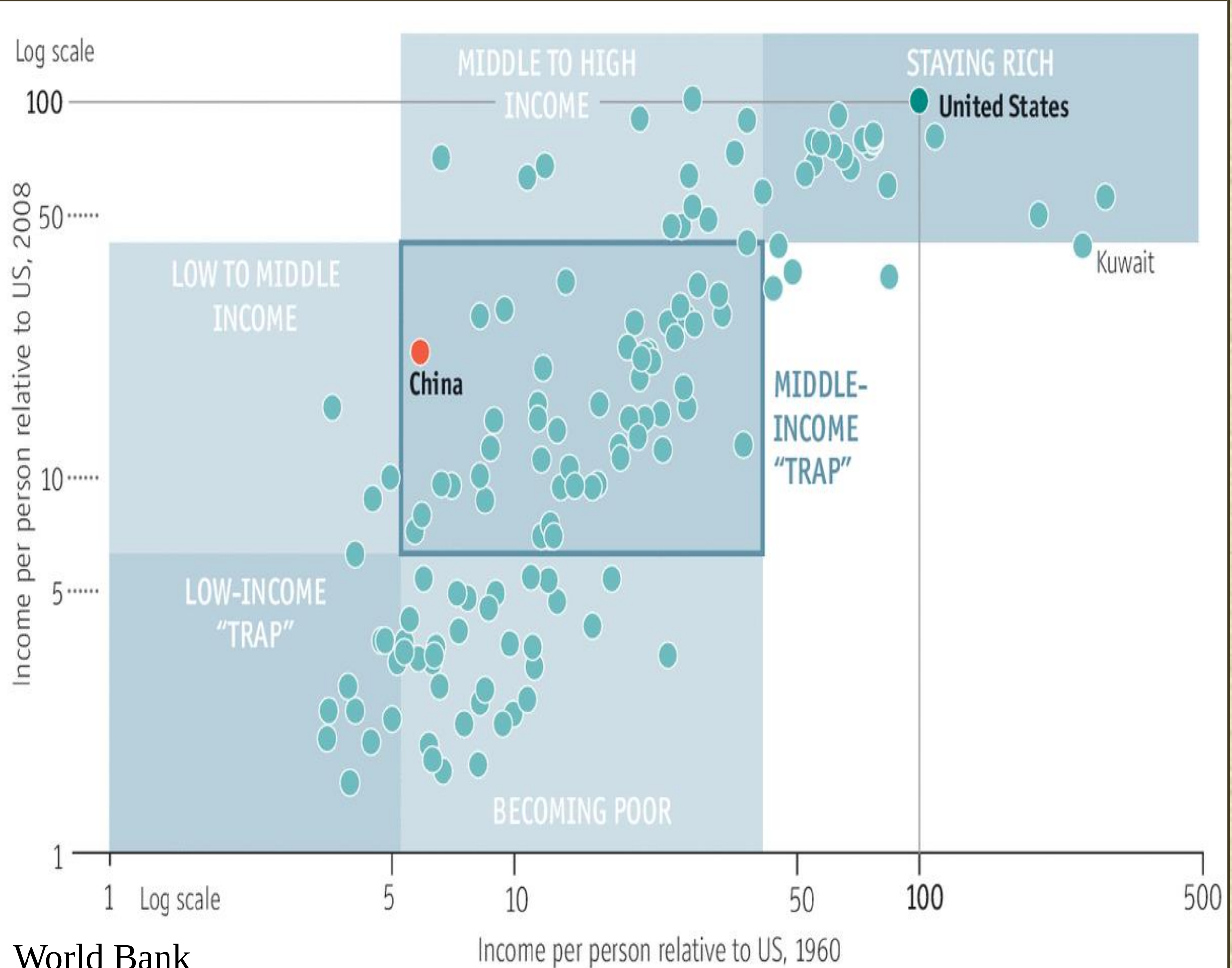
From 1990s-2012, 73% of developing countries out-grew the US by 3.3% a year, on average. Brazil, Russia, India and China had most impressive growth rates, growing in different ways for different reasons.

Economist, "Emerging economies: When giants slow down", 27 Jun 2013, p. 17-9

Strategic Policy Intervention

- Middle-income trap – link between slower prodvty and econ growth

Income per person relative to US, 1960 vs 2008



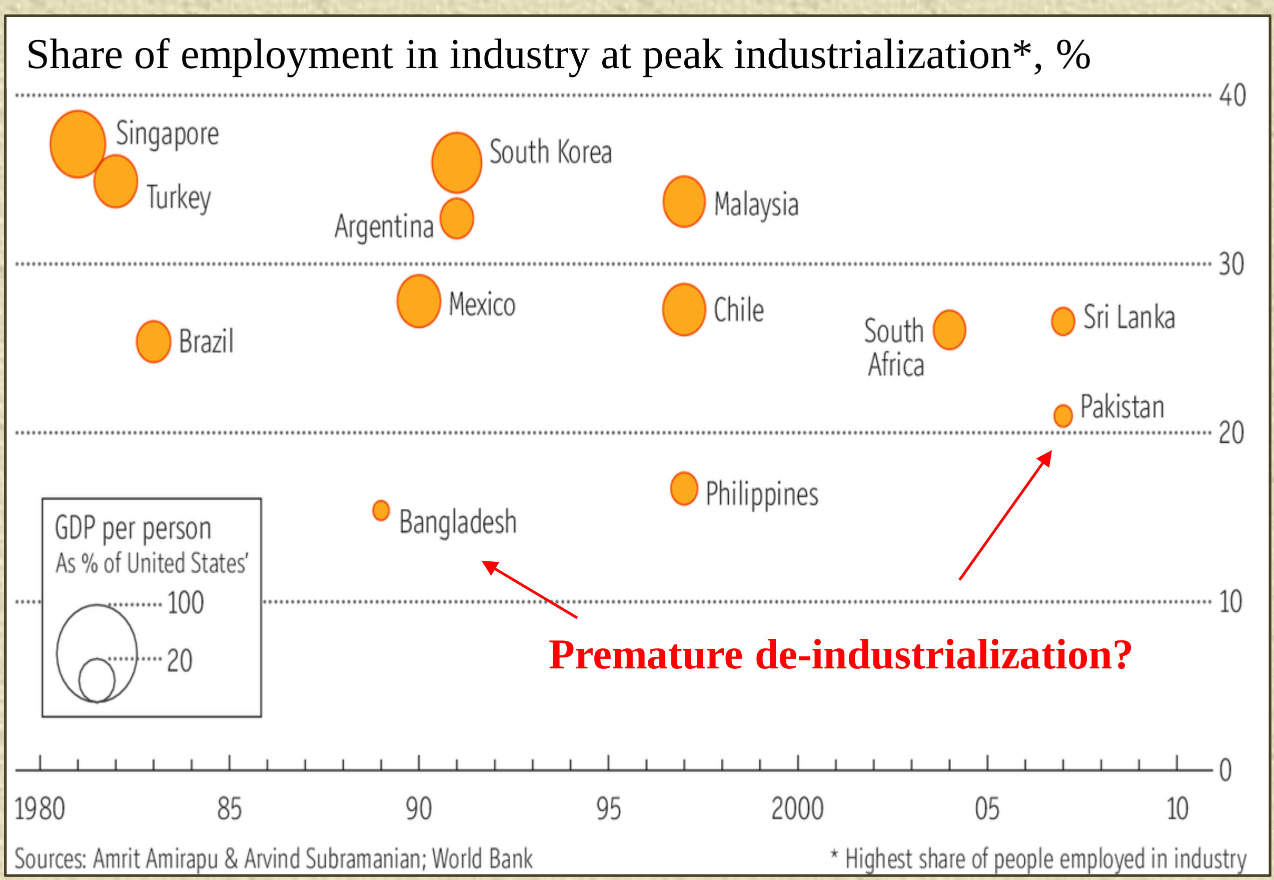
World Bank

Forces of convergence are powerful, but middle-income countries squeezed by high-tech and low-wage rivals on either side. Poorer countries rely on low wages to offset low tech and skills level. They grow faster largely because imitation is easier than invention. The rich need advanced tech and skills to offset high wages. Only 13 countries escaped the middle-income trap from 1960-2008. Averages mask huge variations though.

Economist, Middle-income trap: Mixed-income myths", special report, 7 Oct 2017, 6-8

Strategic Policy Intervention

- Premature de-industrialization
  - Share of employment in manu ↓
  - Manu as % of GDP smaller now



Economist, "Emerging economies: Arrested development", report, on world economy, 4 Oct 2014, p. 11-3

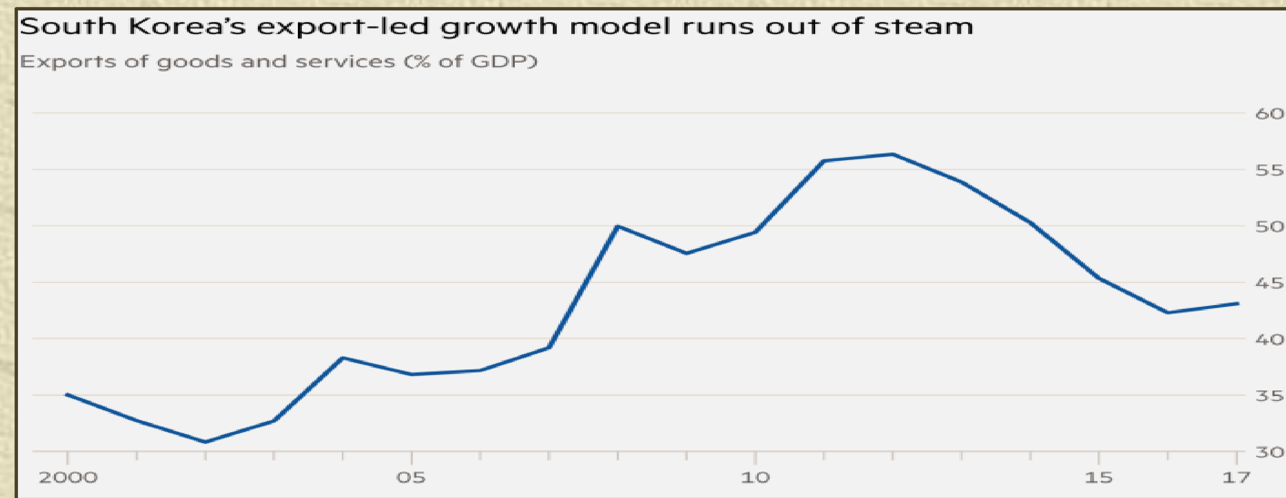
Middle-income economies today employ fewer people in manufacturing than those E. Asian tigers in the 1960s or 1980s.

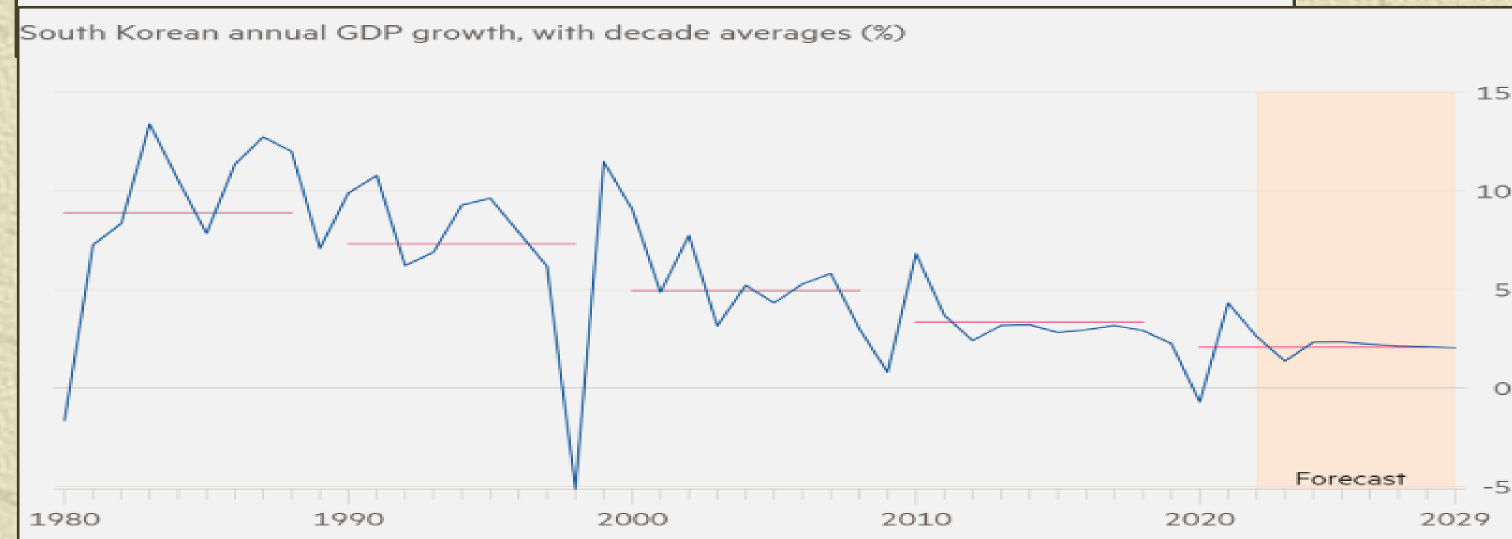
Unless countries can ↑ TFP (R&D): to use L,K more efficiently, create new business org structures, or supply chains, or link manu to D-driven service sectors, growth thru industry slows.

Tech has made it possible for more manu using less less L_M as a % L stock, and at lower GDP levels r.t. US.

Strategic Policy Intervention

- End of the miracle?
  - Case of Korea





State-guided capitalism took it from poor agrarian country to a tech powerhouse in less than 50 yrs. Policy targeted strategic sectors led to tech advances and prodvty gains in the macroeconomy. Two leaps: 1960s-80s from basic goods to petrochemicals and heavy industry; 1980s-2000s move to high-tech manu. The share of sectors in which it was a world leader decreased since 2012.

Financial Times, "Is S. Korea's economic miracle over?", C. Davies, 22 Apr 2024, p. 17.

Financial Times, "In the shadow of a giant", B. Harris, 20 Aug 2018, p. 7.

Strategic Policy Intervention

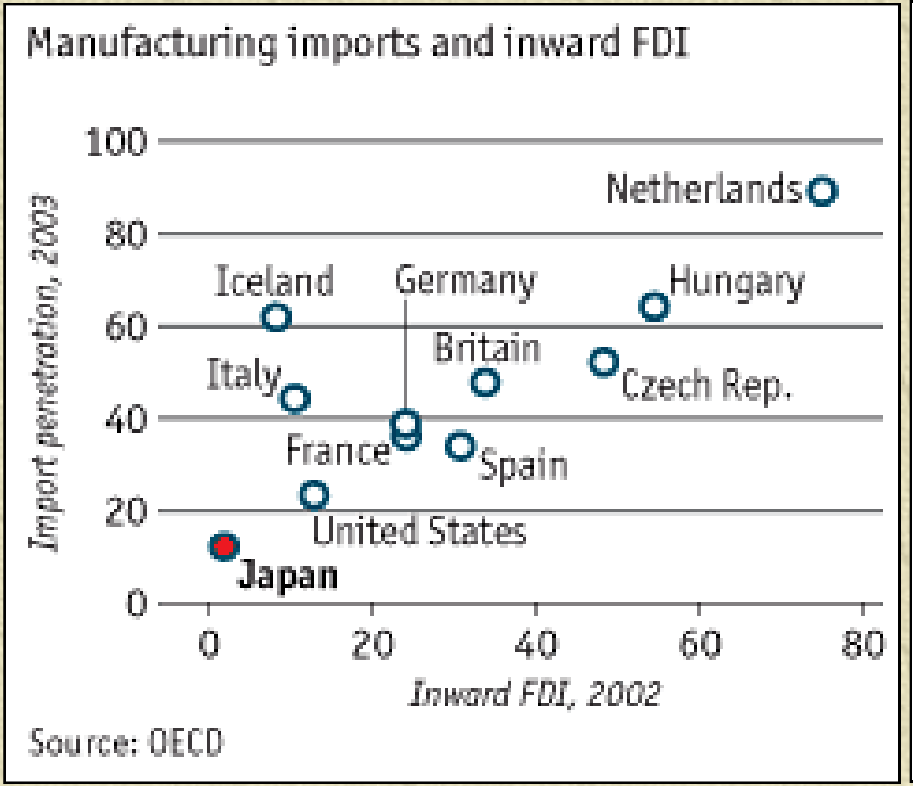
- Japan’s model – export oriented but relatively closed thru domestic regs rather than trade policy
  - Founded on 3 elements for social cohesion and stability
    - Lifetime employment; workers promoted within
    - Seniority-based pay
    - Firm-specific unions: close L-mgmt cooperation
  - Firms - close relationship to a “main bank”
  - “Keiretsu”: firms/subsidiaries linked thru cross-shareholdings

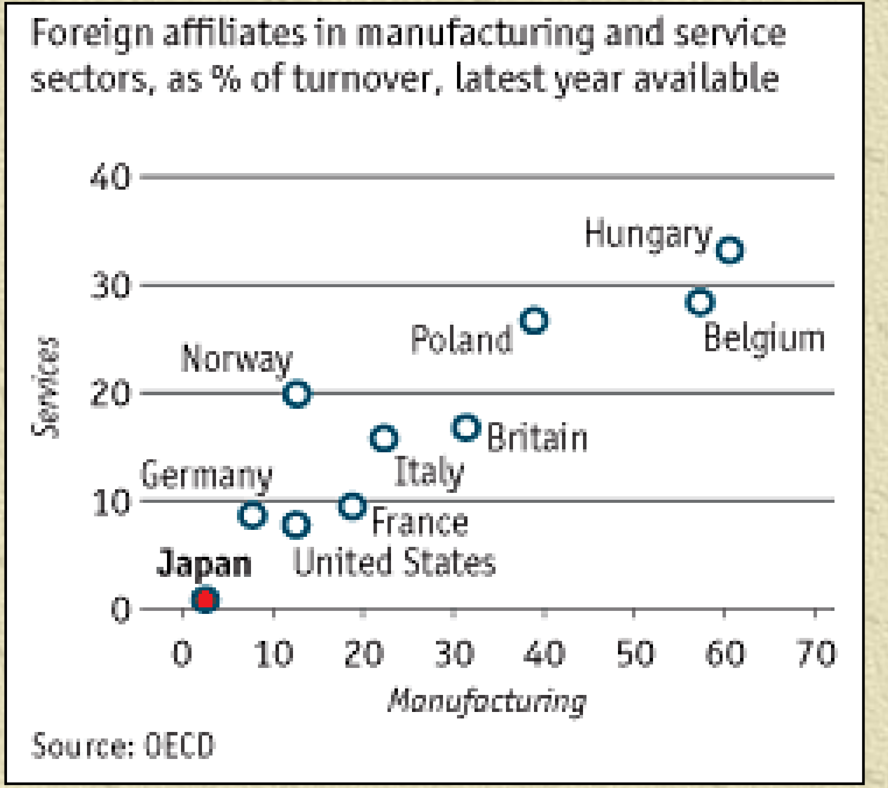
1990s: Japan’s real estate / stock mkt bubble burst - loaded with bad loans. Gov’t thought to be the pillar supporting asset prices.

1997: System collapsed when Bank of Japan declared it could not back private debts. Corporate sector could not restore confidence.

Strategic Policy Intervention

- Downside of the model
  - Lowest level of import penetration and inward FDI – foreigners play little role in its economy
  - Low foreign participation in global wave of cross-border mergers and acquisitions – despite mobility of goods, services, and K

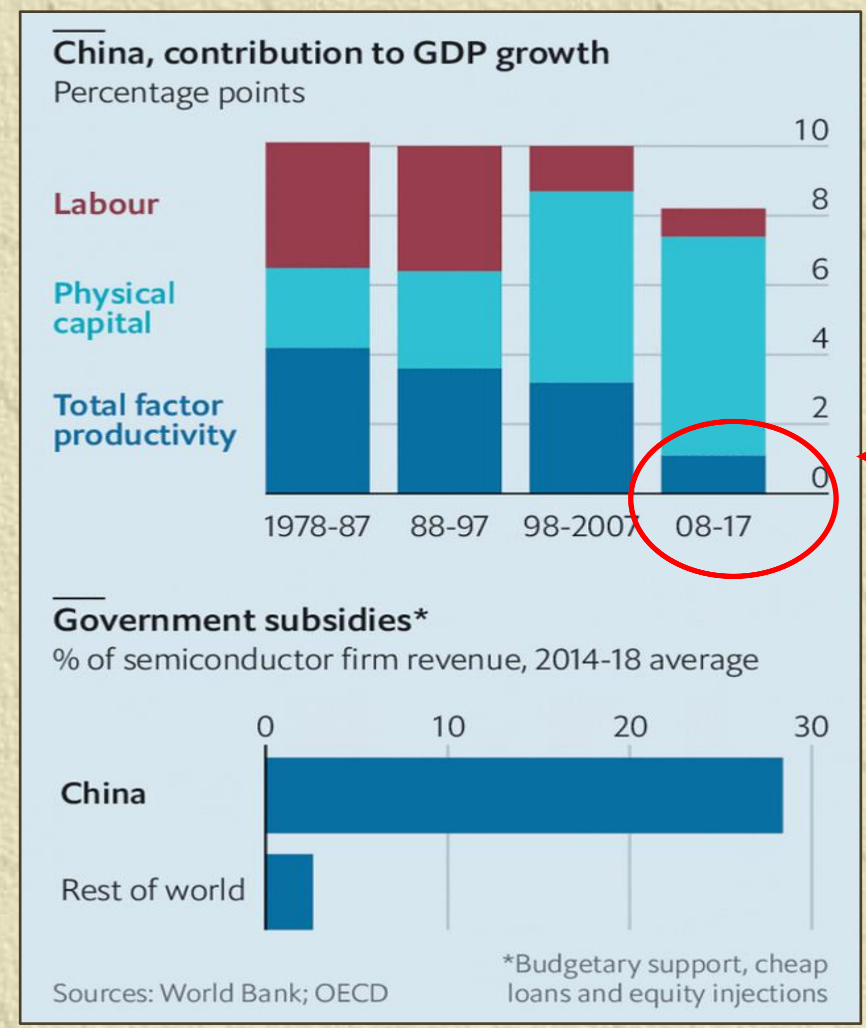




Economist, "No country is an island", and "Going hybrid", 29 Nov 2007.

Strategic Policy Intervention

- China's industrial policy
  - Investment and subsidies



Gov't uses its muscle to stimulate activities not possible by private sector.

Insights from China: (1) industrial policy works better when natural monopolies are involved (high-speed rail; power transmission); (2) continued heavy-handed intervention seems increasingly ineffective in TFP terms.

China's bank-centered, gov't-controlled financial system fostered rapid growth. It has since outgrown the developmental model of finance, adding stock mkts and rating agencies.

2021: ↓ property prices exposed misallocated loans to gov't projects. Corporate debt at 160% of GDP and Bank of China seems unable to deal with bad debt.

Economist, "Free Exchange: Planned Obsolescence", 4 Jan 2020, p. 56.

Strategic Policy Intervention

- Further downside to the strategy

Economist, "Chinese business: Industrial involution", 10 Aug 2024, p. 48-9.

China manufacturers facing problems

Glut in industrial production; 30% of firms were loss-making in Jun 2024 – above the record during AFC.

Subsidies, cheap loans and direct gov't investment have poured into manu, esp in EVs, solar, and semiconductors

8 large makers of cars shut down or stopped prodn since 2023 and some 52,000 EV-related companies (suppliers) shut down, 90% more than in 2022.

Solar industry output is oversupplied and P < avg prodn costs

Semiconductors (low end) also oversupplied

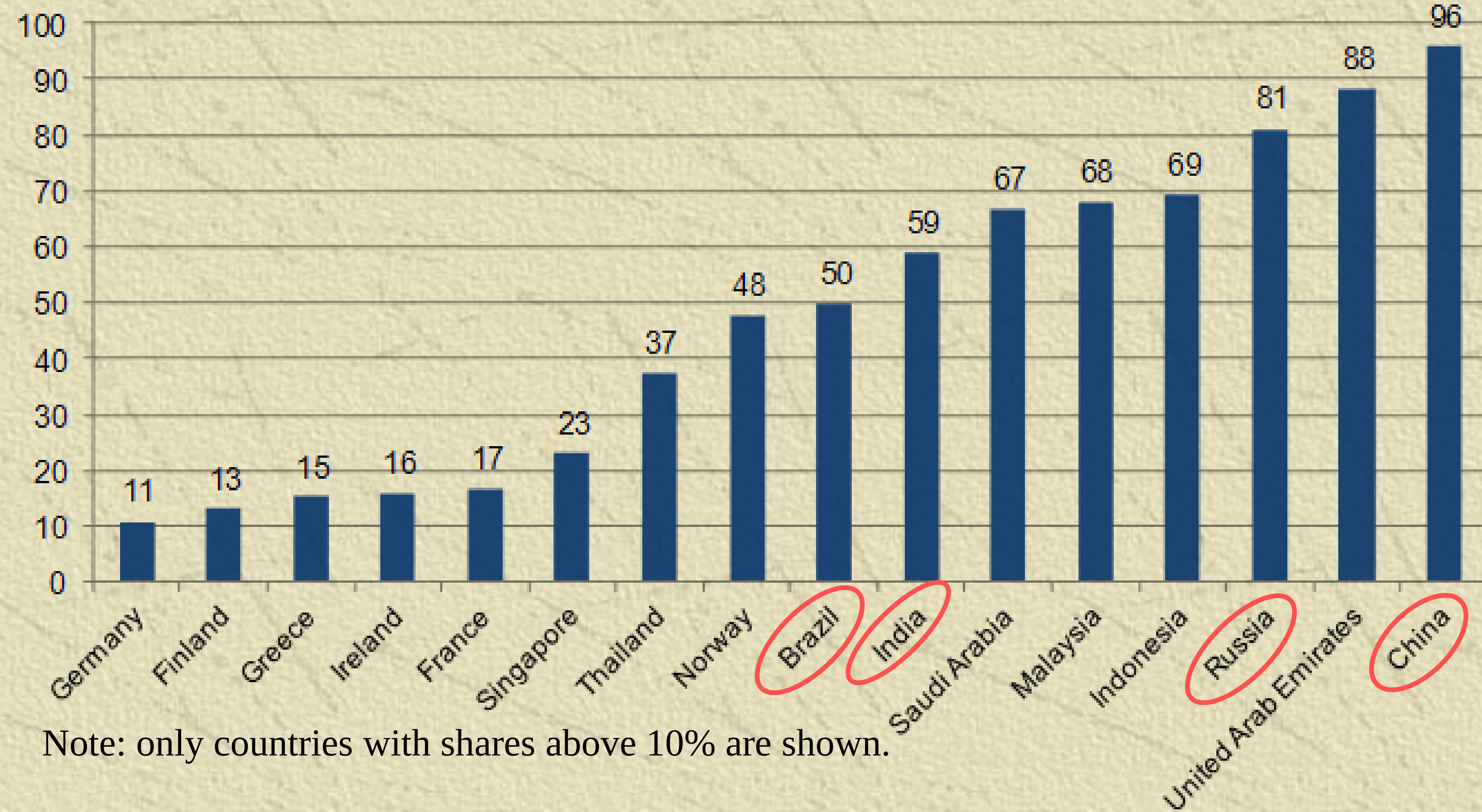
Strategic Policy Intervention

- Neo-developmentalist approach
  - IMF reverses position to allow K-controls and more nuanced on financial liberalization
  - Since global financial crisis (2007)
    - National champions: ↑ investment thru SOEs
    - Internationalization of SOEs: trade and foreign investment
  - Importance of "learning" and economies of scale (EOS)
    - "Mastering" new tech and prodn is a gradual process
    - Requires temporary measures, e.g., protection / subsidies-support
    - Where there are EOS, gov't intervention is justified (even beyond mkt failure argument)

Source: OECD (2015), *State-owned Enterprises in the Development Process*, OECD publishing, Paris. ISBN978-92-64-22961-7   www.OECD.org

Strategic Policy Intervention

- Return to state ownership, 2013
  - State's shares among countries' top 10 firms (%)*



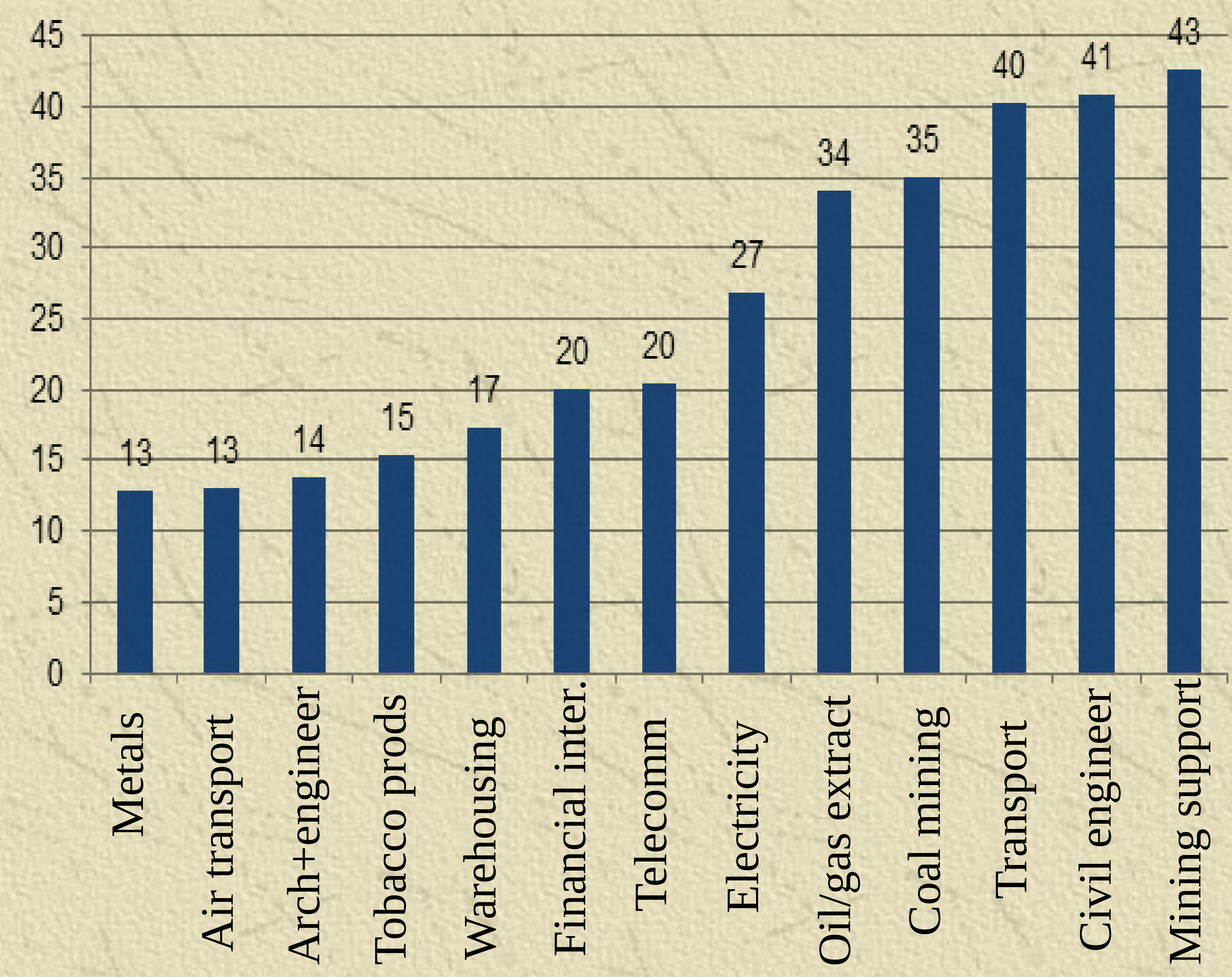
Note: only countries with shares above 10% are shown.

Source: Kowalski, P., M. Büge, M. Sztajerowska and M. Egeland (2013) "SOEs: Trade Effects and Policy Implications", OECD Trade Policy Paper, No. 147.

* Excludes unlisted SOEs such postal services or utilities, and firms with minority state shareholding.

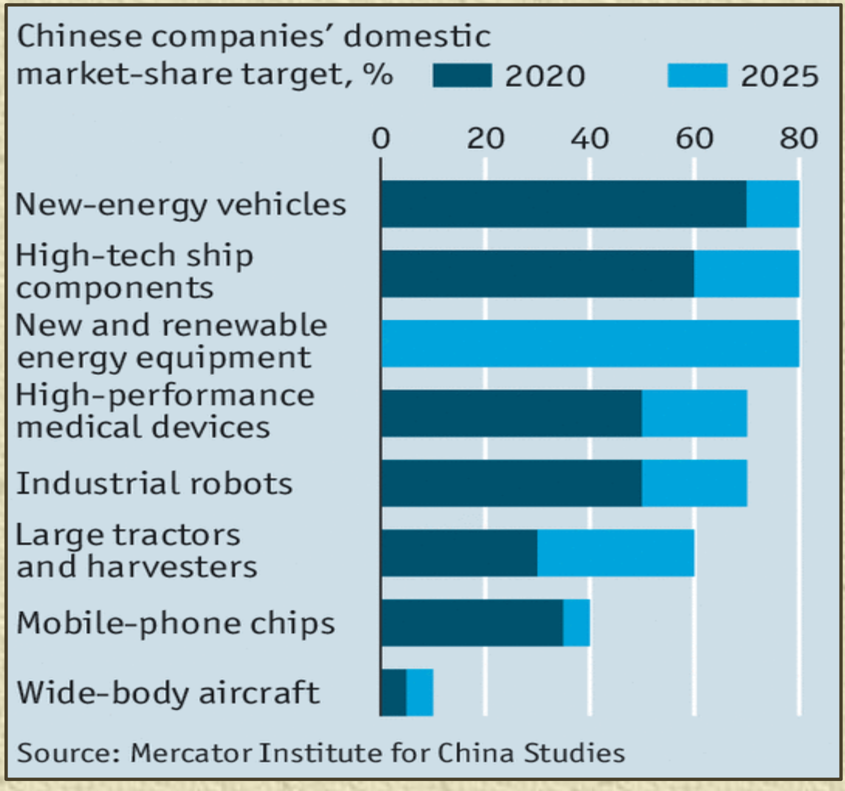
Strategic Policy Intervention

- State ownership, share by sector (%)



Strategic Policy Intervention

- Industrial policy in China "Made in China, 2025"
  - 1,013 state-guided funds endowed with 5.3 trn yuan ($807bn)
  - Manufacturing subsidies spread over 62 separate initiatives
  - Market share targets both at home and abroad
  - Local content rules – also illegal under WTO rules



Economist, "China's economy: Biting the Bullet", 23 Sep 2018, p. 61-2.

Strategic Policy Intervention

- Beijing consensus – China model
  - Features from S. Korea and Taiwan
    - X-led: BOT surplus for 3 decades
    - Investment: gross fixed K formation at 42% GDP
    - Closed K acct limits K-outflows
    - i-rates artificially low (low returns for savers too)
    - Cheap bank financing for industry favored by state
  - Distinctive Chinese features
    - Korea and Taiwan moved from autocratic to democratic rule at lower level of GDP/cap; China still autocratic
    - State economic power used for political ends
    - 50% of bank assets held by state-owned lenders
    - Use of special economic zones – tax breaks and liberal investment rules

Economist, “Autocratic admirers: Painting the globe red”, 8 Jun 2024, p. 61-2.

Strategic Policy Intervention

- Followers of the China model

China model, score of 1=highest level in given category, 2023 or latest

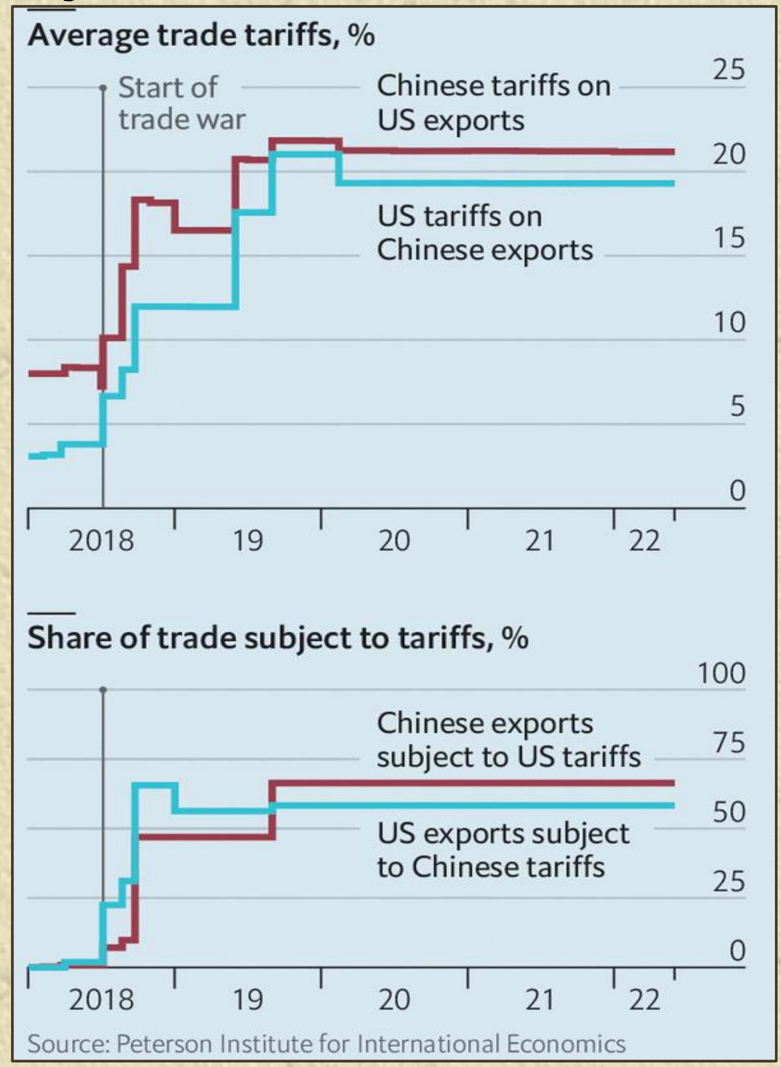
Country* (Overall score†)	Capital-account restrictiveness‡	Authoritarianism§	Gross fixed-capital formation**	Manufactured goods, as % of exports	Government-owned bank assets††
1 Vietnam (0.67)	0.58	0.93	0.62	0.86	0.70
2 Russia (0.61)	0.84	0.98	0.28	0.22	0.88
3 India (0.60)	0.84	0.34	0.54	0.62	1.00
4 Bangladesh (0.60)	0.84	0.51	0.64	0.96	0.41
5 Turkey (0.59)	0.84	0.71	0.53	0.74	0.50
6 Ethiopia (0.58)	0.84	0.83	0.62	0.09	0.90
7 Pakistan (0.51)	0.84	0.85	0.05	0.75	0.30
8 Angola (0.51)	1.00	0.73	0.35	0.01	0.44
9 Azerbaijan (0.51)	0.54	0.91	0.22	0.03	0.59
10 Indonesia (0.50)	0.58	0.42	0.63	0.43	0.59
21 South Korea (0.44)	0.00	0.22	0.63	0.85	0.36
49 South Africa (0.29)	0.84	0.36	0.08	0.37	0.00
77 Georgia (0.20)	0.00	0.60	0.34	0.34	0.00
85 Greece (0.10)	0.00	0.22	0.00	0.34	0.00

*Out of 85 countries †Average of seven categories. Current-account-surplus and special-economic-zones measures not shown
‡Based on the China-Ito index §Uses EIU's democracy index **As % of GDP ††As % of total bank assets
Sources: Chinn-Ito index; EIU; IMF; UNCTAD; World Bank; *The Economist*

Strategic Policy Intervention

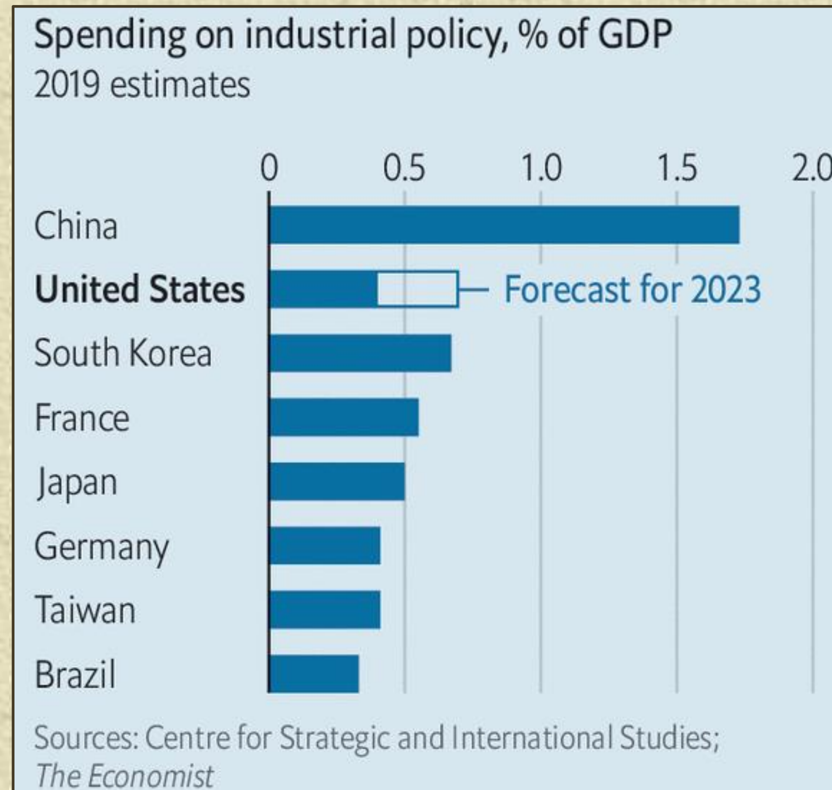
8.3 Policy intervention in developed countries

- WTO constrains use of trade policy and subsidies
  - Tariff ceilings are low, on avg
  - Trump's trade war; Biden follows
    - Tit-for-tat tariff escalation
    - Violation of WTO rules



Strategic Policy Intervention

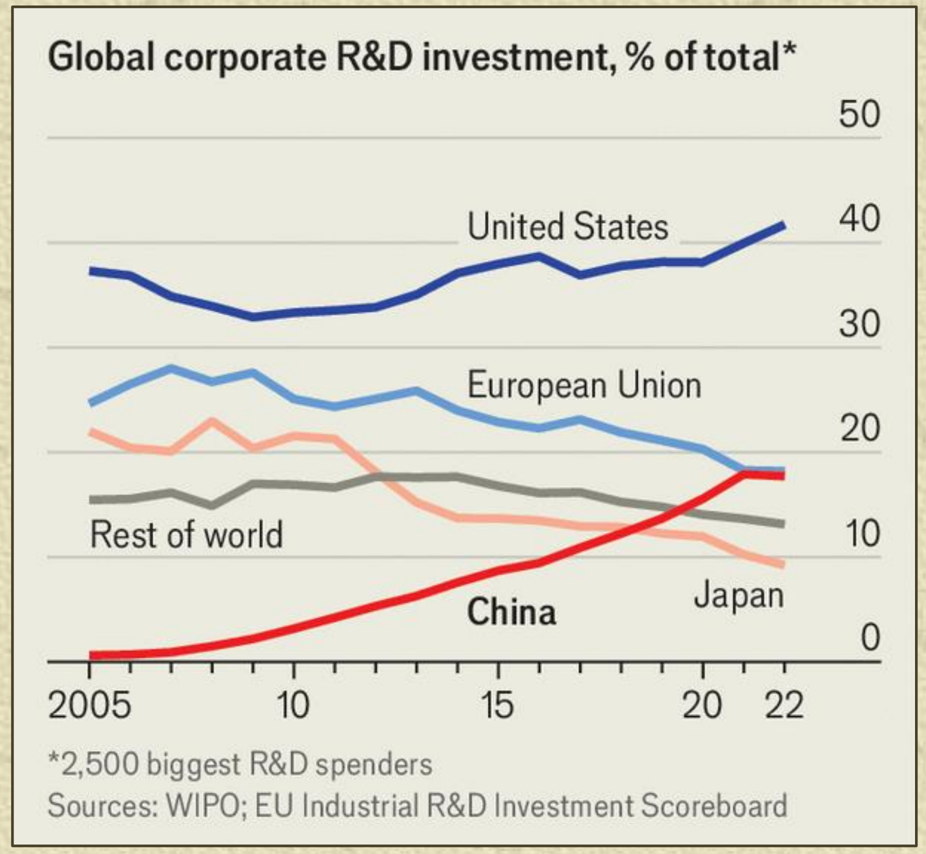
- Industrial subsidies prohibited under WTO, except
  - 75% of research costs
  - 50% of new prod develop
  - Infrastructure
- West embraces industrial policy
  - US subsidies matched by EU
  - Violation of WTO rules



Economist, "Adieu, laissez-faire", Briefing on Bidenomics, 29 Oct 2022, p. 21-3.

Strategic Policy Intervention

- Cases for gov't intervention of North
  - Infant industry argument applied to R+D-intensive sectors



Economist, "Innovation: Research developments", 20 Jul 2024, p. 49-50.

China becoming world's R&D laboratory. Between 2012-21, foreign firms increased hires of Chinese research personnel by a fifth. Annual R&D spending in China doubled. Add investment by local firms and China matches EU's R&D tally. Only US spends more.

Examples of western R&D in China:

* VW: invested more than $1bn in an innovation center

* HSCC: UK bank affiliated with an R&D center working on uses of AI, block chains and biometrics

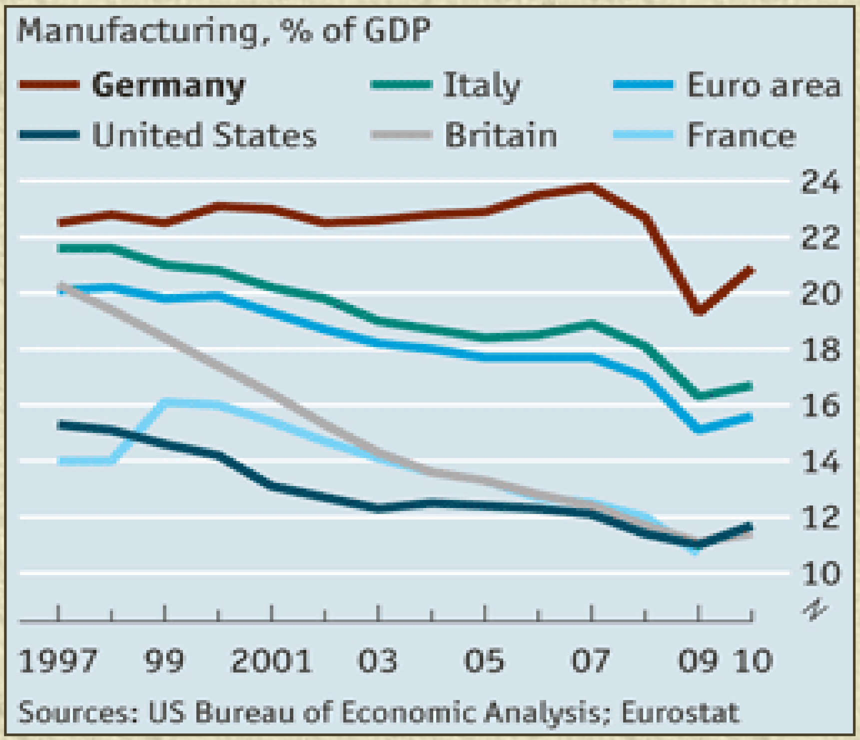
* AstraZeneca: UK pharma firm has global R&D hub

* Tesla – testing most advanced autonomous driving systems

Strategic Policy Intervention

- Externality argument: de-industrialization from North-South trade
  - Manufacturing shares

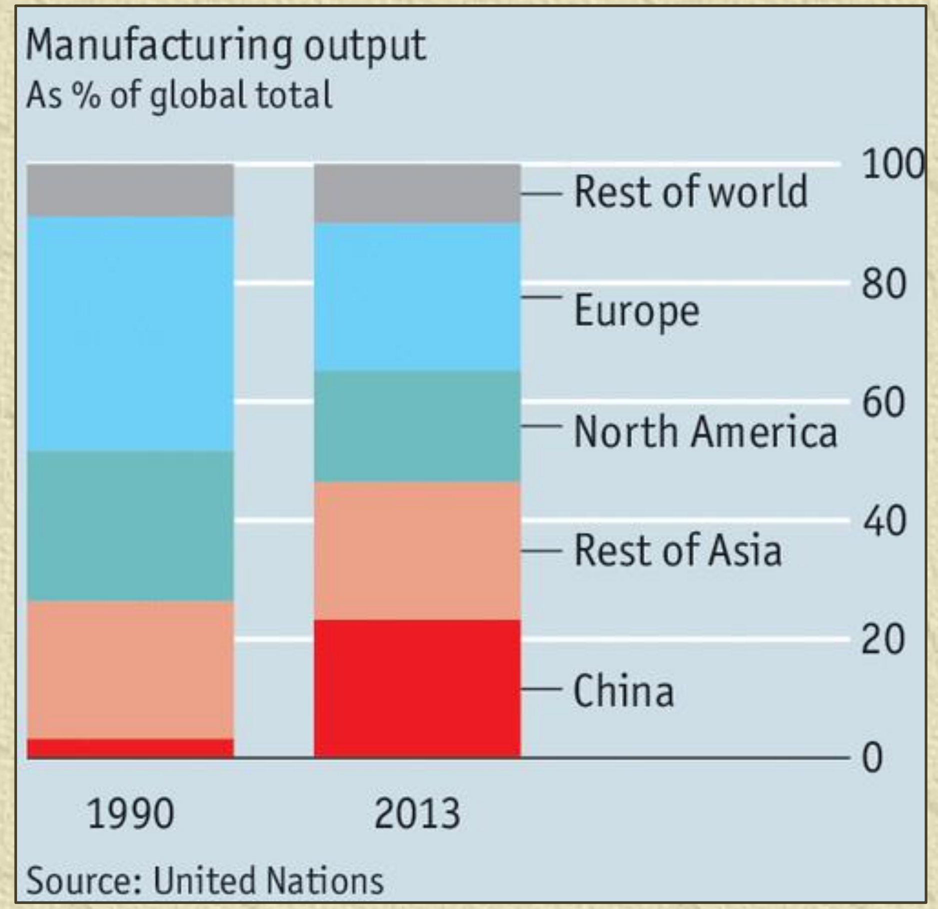
Economist, "Manufacturing: The new maker rules", 24 Nov 2012, p. 66-7.

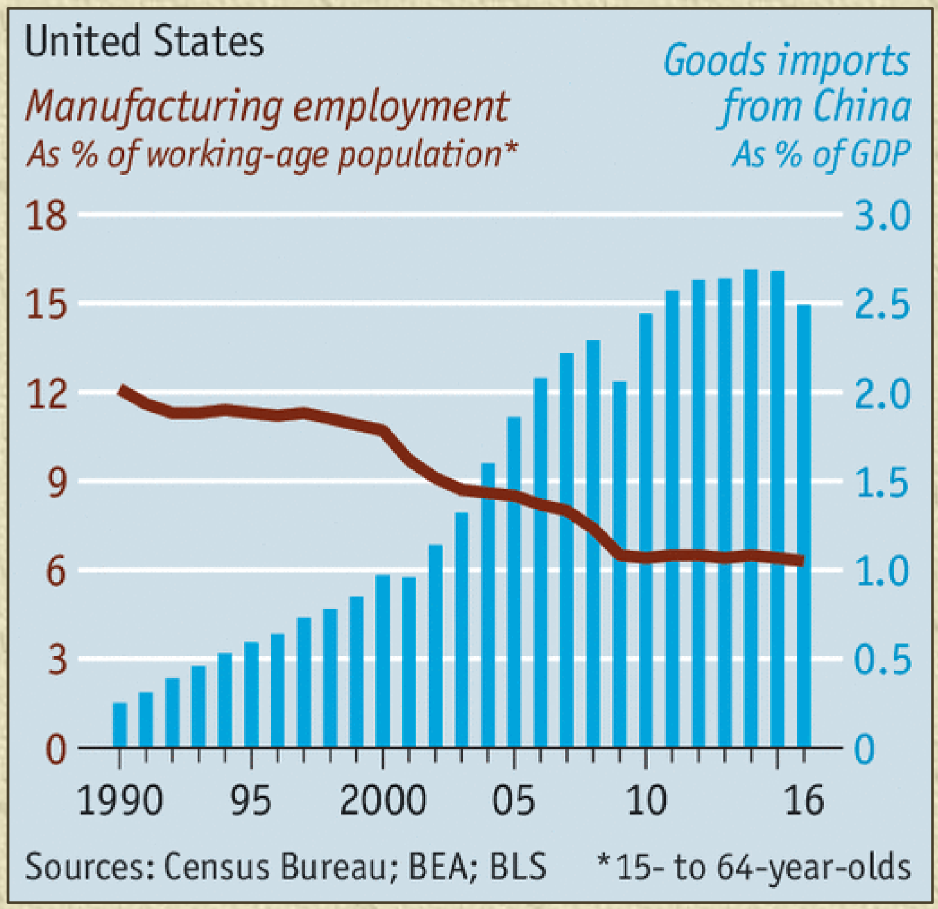


Economist, "What Germany Offers the World ", 14 Apr 2012, p. 56.

Strategic Policy Intervention

- US-China trade and US employment in manufacturing





Economist, "The future of factory Asia: A tightening grip", 14 Mar 2015, p. 61-2.

Source: *Economist*, "Trade with China: Shock horror" 11 Mar 2017, p. 70

Strategic Policy Intervention

- Relative productivity: manufacturing

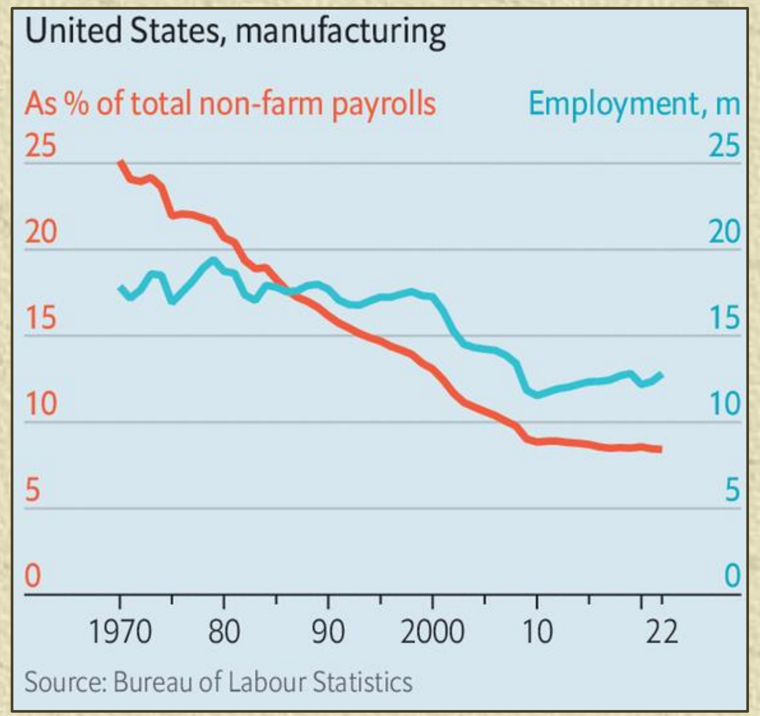
Source: *Economist*, "Manufacturing: Making it in America" 14 Oct 2017, p. 55.

Many reckon that global trade, especially with China, is to blame for the loss of manu employment. Studies show majority of past factory job losses were result of investment in automation (tech). Output more than doubled in real terms. Output per labor-hr rose 47% between 2002-15.

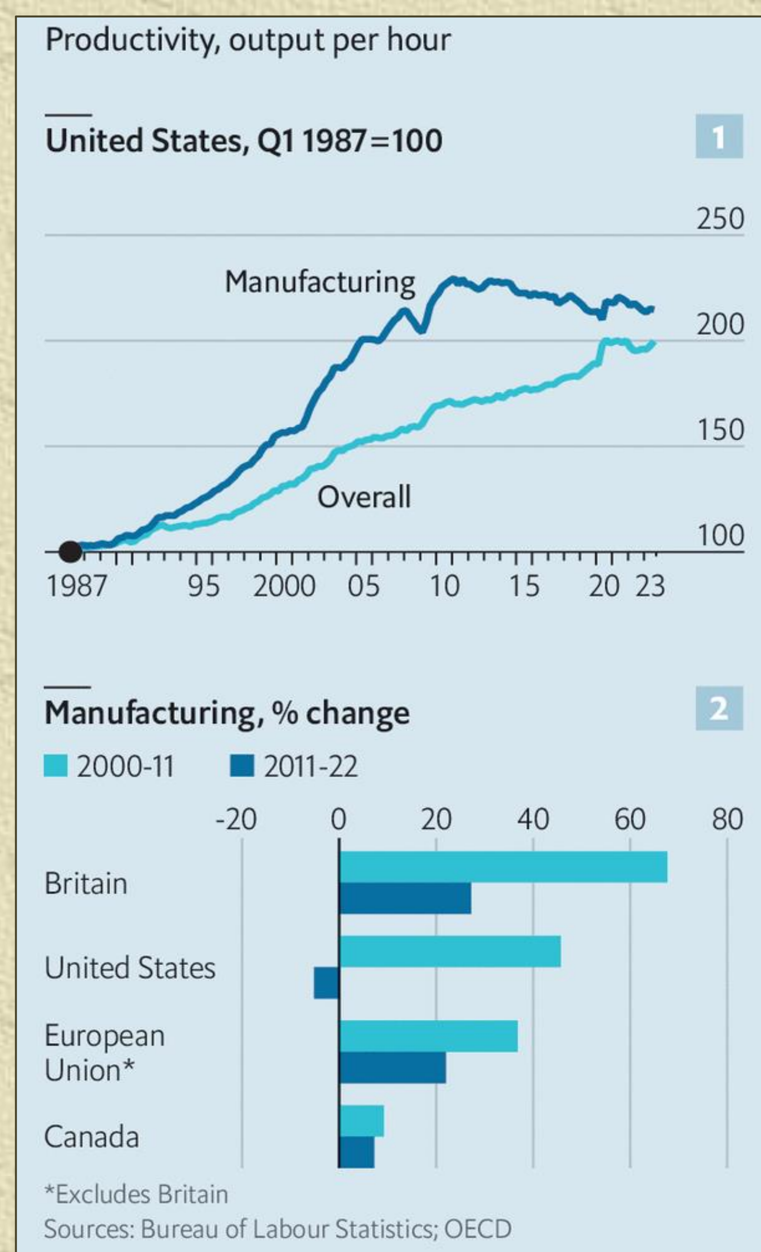
When Taiwan's Foxxconn, the world's largest contract manufacturer, which employs over 1m people in China, stated it would build a factory in the US employing up to 13,000 people in return for **$3bn in tax breaks and state subsidies**, Mr. Trump called a press conference to celebrate ($230,769/job).

Strategic Policy Intervention

- Reduction in US manu since 2011



Source: *Economist*, "Reindustrialising America: Rosy for riverters" 04 Febov 2023, p. 16-9.



Source: *Economist*, "Manufacturing problems: About that renaissance" 11 Nov 2023, p. 69.

Strategic Policy Intervention

- Relative productivity manufacturing and services

Substituting labor for capital is more difficult in services. Some services sub-sectors are more labor intensive than others.

Thus, labor's share in the services sector is expected to increase relative to manufacturing.

- Services growth: alternative explanation to de-industrialization

Economist, "German Services: Protected and Inefficient", 18 Feb 2012, p. 24.