Regimes of Underdevelopment – Why is there almost no convergence in the world economy

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Only a small number of countries managed to reach real GDP per capita levels comparable to developed countries.

Successful countries are: Japan, Taiwan, South Korea, Singapore, Hong Kong.

Why is there no convergence?
Real GDP per capita in per cent of US GDP per capita

Source: Penn World Tables 7.1
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How to explain the lack of convergence traditionally

- Friedrich List – free trade “kicking the ladder away”

- Prebisch–Singer Hypothesis – terms of trade

- Dutch disease and resource curse – the problem of natural resource rich countries
Do developments after the begin of the neoliberal area in the 1970s improve development chances?
Global value chains

- A revolution in international trade – tasks no complete goods
  - Washington consensus – open up for foreign direct investment
  - Revolution in transportation technology
  - Revolution in information technology

- Key role of multinational companies
Over the last decades the smile curve became deeper. Over the last decades low value creating activities are outsourced to developing countries.
Premature de-industrialisation (Dani Rodrick)

- Maximum share of industry is reached in developing countries much earlier than in now developed countries and successful developing countries

- Lack of a dynamic sector for development (Can the service sector take over this function in developing countries?)

- No traditional working class is created – no political power for more equal wages and welfare state
Low quality currencies and at the bottom of the currency hierarchy

- Deeper integration in international financial markets
- Portfolio diversification and capital flights by elites in developing countries and dollarisation
- Schumpeterian–Keynesian credit–investment–income–creation mechanism is stopped by capital exports
- Boom–bust cycles of international capital flows and original sin
Increasing and /or very high inequality

- Financialisation increases inequality also in developing countries
  - Developing countries have higher real interest rates
  - Shareholder value corporate governance
  - Weaker trade unions, informal sector, etc.

- High inequality prevents long growth periods
  - Negative demand effects
  - Negative supply effects
Foreign direct investment (FDI) as big hope

- FDI can transfer some technology, skills and export markets

- FDI without domestic forward and backward linkages and creating clusters has limited effects

- Other negative effects of FDI
  - Not in all sectors is FDI useful (for example real estate sector, financial sector, natural monopolies, ...)
  - Crowding out promising domestic companies
  - Transfer of profits abroad
  - Increasing inequality
Conclusion

- The neoliberal area has made anyway difficult catching up more difficult

- Only a small group of countries will be able to catch-up – probably only China and India have a chance

- Others will be integrated in the global economy at different levels of under-development

- And all of this without discussing domestic problems of many developing countries (rent-seeking elites, weak institutions, ...) and that developing countries may be less able to protect themselves against ecological catastrophes
Ecological problems as a fourth development trap

- Developing countries are more affected by ecological problems than developed countries.

- Developing countries have less capacity to compensate and fight against consequences of ecological changes.
What to do?

- The precondition for development is the creation of institutions and the political will to solve the three traditional factors which lead to a development trap.
- Comprehensive regulations of markets is needed including a regulated integration into the world economy.
- Development aid has more negative than positive effects (Edward Webster: Give the man a fishing rod not a fish).
- Developing countries should follow a policy of ecological change with technical revolution and growth.
Literature