

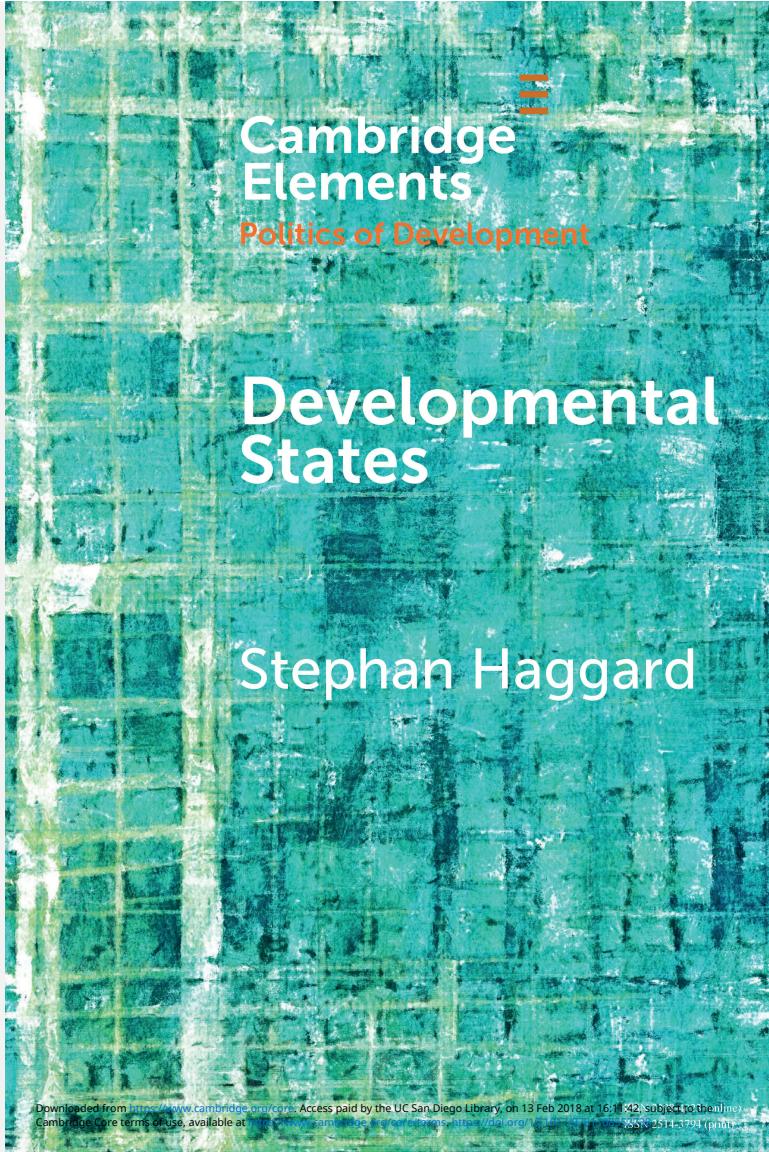
DEVELOPMENTAL STATES: LESSONS FROM EAST ASIA

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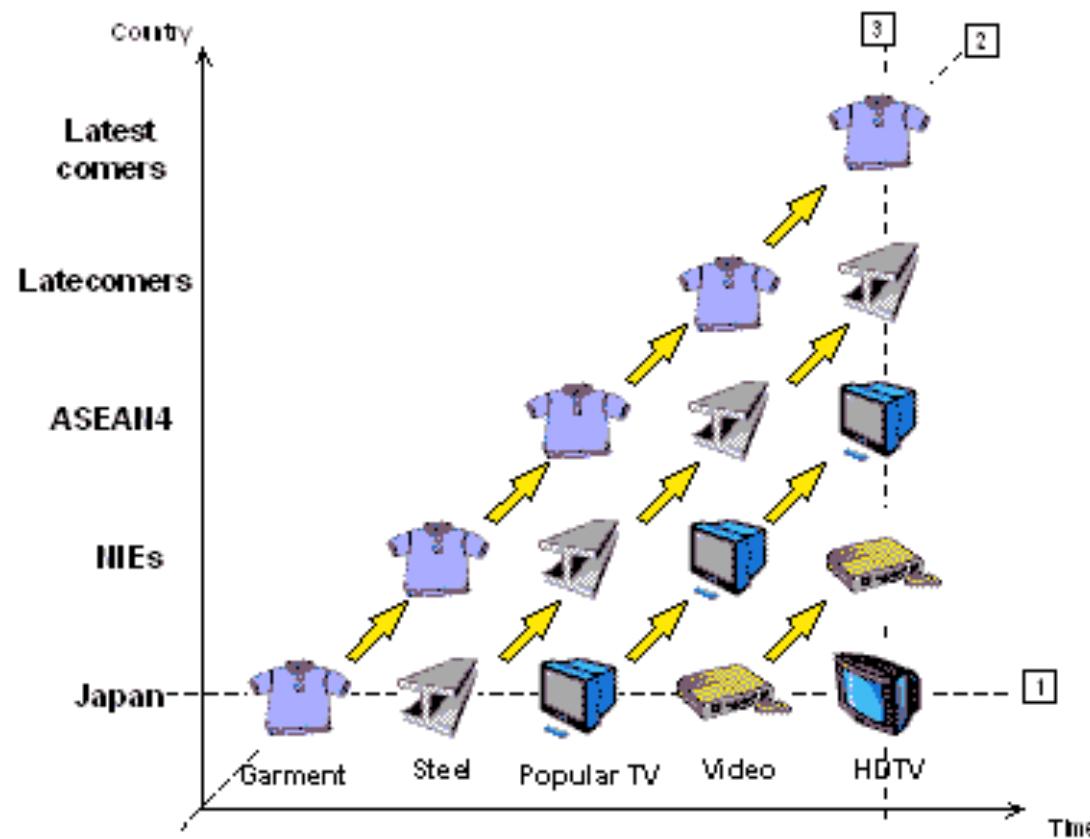
Developmental States

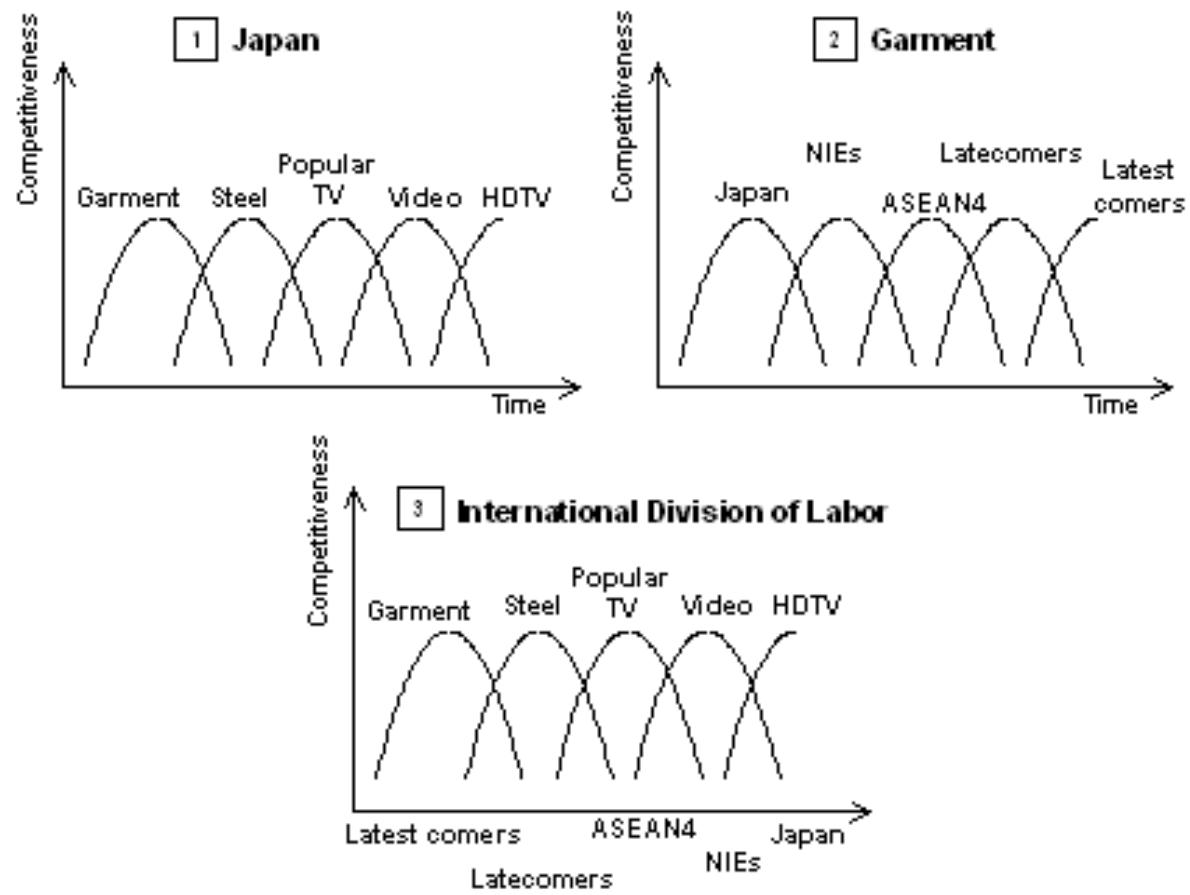
- As a summary of the East Asian experience
- As a heterodox institutional approach to long-run growth



- High growth episodes...
 - Japan: ~1950-1973
 - Korea, Taiwan, Hong Kong and Singapore: from ~mid-1960s
 - Malaysia (Penang), Thailand, Indonesia: from ~1970s
 - Vietnam and China: from ~1980s
- Associated with transitions to export-oriented growth...
- ...but also large inflection in private investment

Structural Transformation in East Asia





THE ECONOMIC DEBATE

- The neo-classical view
 - Transitions to export-oriented growth were *primarily* the result of trade and exchange rate reforms...
 - ...that shifted incentives for both domestic and foreign firms
- The heterodox view
 - Market failures prevent liberalizing reforms from having desired effects
 - State intervention—**in effect, the creation of rents**—was critical to jump-start not only exports but *private investment*

COORDINATION PROBLEMS

- The challenge of development is in overcoming *coordination problems*
 - In transition from agriculture to industry (“traditional” and “modern” sectors), and thus in *industrial policy*
 - An example from Rodrik
 - With respect to the financial sector: *assuring access to credit* (Stiglitz)
 - With respect to technology and learning: *bargaining with foreign firms with respect to technology transfer*
 - Coordination leads back to the role of efficient and effective state intervention

RODRIK ON THE COORDINATION PROBLEM IN THE REAL SECTOR

- “From the perspective of an individual investor it will not pay to invest in the modern sector unless others are doing so as well. The profitability of the modern sector depends on the simultaneous presence of the specialized inputs; but the profitability of producing these inputs in turn depends on the presence of demand from a pre-existing modern sector. It is this interdependence of production and investment decisions that creates the coordination problem. (1995, 79–80)
- Industrial policy councils in Japan, for example, in steel

THE SHIFTING ECONOMIC LANDSCAPE

- The (larger) developmental states combined import-substitution with export-oriented growth: is this still feasible? *Probably not.*
- Pressures on the old-developmental state model
 - Pressures from advanced industrial states and IFIs to liberalize
 - Financial crises—particularly in 1997-98--compound these pressures
 - The growth of export-oriented foreign direct investment and international production networks demands openness

QUESTIONS FOR AFRICA ON THE ECONOMIC MODEL

- Questions
 - What are target industries?
 - Who are target competitors? For example, Bangladesh and Vietnam.
 - Who are target investors, including China?
 - Where are target markets, including in Africa with CFTA?
- *Send staff to those countries, not to Washington.*

MORE QUESTIONS FOR AFRICA ON THE ECONOMIC MODEL

- Are you building on earlier import-substitution by *domestic firms* (Japan and Korea), or relying more heavily on *entry into international production networks* (Singapore and Penang)?
 - If former, the coordination problem centers on facilitating entry into foreign markets: **finding buyers, intermediaries or brokers**
 - If latter, the key relationships are not only with foreign firms...
 - ...but between those firms and workers (**Penang Skill Development Center**) and *potential domestic suppliers* (Singapore's efforts at "matchmaking," linkages and upgrading)

**ABOVE ALL, WHAT ARE *YOUR*
COORDINATION PROBLEMS?**

THE DEBATE OVER INSTITUTIONAL AND POLITICAL FOUNDATIONS

- A dominant neoclassical view centered on property and contracting rights, rule of law and ultimately constitutional and judicial checks on government
 - The Asian anomaly
 - The heterodox alternative
 - Strong, insulated but incentivized bureaucracies: the focus on *investments in state capacity*
 - The importance of *discipline*: mechanisms for consulting with the private sector but controlling rent-seeking

POLITICAL FOUNDATIONS I: INCENTIVIZING BUREAUCRACIES

- Almost all of the developmental states except Japan were authoritarian or semi-democratic
- But rulers **delegated substantial authority to centralized bureaucratic “lead agencies”** such as MITI (Japan), EPB (Korea), Economic Development Board (Singapore)
- **Undertook bureaucratic reforms to incentivize civil servants**
 - Internal systems of both rewards (such as competitive pay, long-term career tracks) and controls (merit-based promotion; sanctions for corruption)
 - Investment in expertise: not just macroeconomic policy, *but industry-level knowledge*. A Singapore example: the disk-drive industry.

POLITICAL FOUNDATIONS II: THE PRIVATE SECTOR AS A SOURCE OF RISK

- Neoclassical models of politics
 - Generally focus on *government failures* and *risks of state intervention*
 - Largely see the private sector as benign
- Heterodox models focus on *risks emanating from the power of private actors, including both foreign and domestic firms*
 - Capture, bribery and corruption at home...
 - ...but also excessive demands from foreign firms as well

POLITICAL FOUNDATIONS II: THE PRIVATE SECTOR AS A SOURCE OF RISK

- Government needs information from the private sector, and a number of developmental states used *business councils* to elicit information (Rodrik)
 - Assuring that representation includes competitors
- Yet at the same time, rents extended to the private sector were *conditional on performance*...
 - Alice Amsden's concept of “discipline”
 - ...using mechanisms such as *contests* in which policy benefits were made conditional on some metric of performance (for example, exports)

RODRIK ON INDUSTRIAL POLICY

- “The task of industrial policy is as much about eliciting information from the private sector on significant externalities and their remedies as it is about implementing appropriate policies. The right model for industrial policy is not that of an autonomous government applying Pigovian taxes or subsidies, but of strategic collaboration between the private sector and the government with the aim of uncovering where the most significant obstacles to restructuring lie and what type of interventions are most likely to remove them.”

AMSDEN ON DISCIPLINE

- “A control mechanism is a set of institutions that imposes discipline on economic behavior. The control mechanism of “the rest” revolved around the **principle of reciprocity**. Subsidies (“intermediate assets”) were allocated to make manufacturing profitable – to facilitate the flow of resources from primary product assets to knowledge-based assets – but did not become giveaways. **Recipients of subsidies were subjected to monitorable performance standards that were redistributive in nature and results-oriented** (Amsden 2001)

QUESTIONS FOR AFRICA ON THE POLITICAL MODEL

- Is state structure appropriate to achieve your goals?
 - Delegating to "pockets of excellence" within the state which are capable of coordinating across ministries
 - Undertaking bureaucratic reform to enhance capacity, including industry-specific knowledge
- Do business-government relations support the approach?
 - Does the government have channels for input from the private sector?
 - Does the government have strategy for limiting corruption, but also making rents conditional on performance?

QUESTIONS FOR AFRICA ON THE POLITICAL MODEL

- As African countries transition to democratic rule, how do we forge coalitions in support of developmental states?
- Increasing evidence that African voters—like voters everywhere—are interested in performance (and not, for example, only about ethnicity or clientelism)
 - Building political support for the model
 - An East Asian paradox: although repressive toward the left and labor, also undertook extensive land reforms and invested heavily in human capital

QUESTIONS FOR AFRICA ON THE POLITICAL MODEL

- Should we be thinking about the developmental state at the national level...
- ...or at “developmental provinces” and “developmental cities” that are empowered to experiment?
 - Penang
 - The Chinese experimental approach to export-processing zones and other policy innovations

**BEWARE OF FOREIGN MODELS!
DEVELOPMENT IS ULTIMATELY A
LEARNING PROCESS.**