Liberal Theories of Economic Development

http://www.gapminder.org/videos/hans-rosling-ted-talk-2007-seemingly-
The Global South: developing or underdeveloped...”emerging markets” or just poor countries?
Today’s Agenda

• Is the World Developing or Underdeveloped?
  – The good news: Growth and aggregate improvement in human welfare indicators
• Liberal views on development and explanations for the growing gap
  • A. Rostow and Stages
  • B. Liberalism and integration into the international economy:
    – Staples Theory (Trade)
    – Product cycle (MNC),
    – Institutions
• C. Internal Requirements for Development
  – Move from a traditional to a modern society
  – Democracy
• D. Summary of the Liberal position
Theory-based Terms: The words contain the theory

- Liberal Theory
  - Developing countries
  - Less Developed Countries
  - Emerging markets
- Dependency theory
  - Underdeveloped Countries
- Neutral?
  - The Global “South”
What is economic development?

• Overall growth?
• Emphasis on consumption and income levels?
• Or maximizing people's capabilities--that is, their ability to lead the kind of life they value.
• But does this definition depend on economic growth?
• Yes
  – Most of the theories of development say so
Who is North and Who is South?

- North = World’s Rich
- South = World’s poor, or developing nations, or emerging markets (more complicated)
  - Used to be called the Third World
  - We can no longer lump together the countries of the “south”
  - Some are growing and “emerging” and some are not.
The Good News

- 20th century economic output off the charts!
- South Korea and China doubled productive output in 10 years
- Humans are, on the whole more healthy now than 100 years ago.
Health and income have improved

[allCountries.swf]

Liberal explanations for global growth

• Walt Rostow: the intellectual context
  – No previous conceptual apparatus
  – But experience with Marshall Plan
  – But there were historical patterns of development
  – Winning the cold war meant:
    Helping the “Third world” develop
    Within the liberal capitalist model
Stage 1: Traditional society

• Why no growth?
Stage 2: Preconditions for Growth

- Population growth will outpace economic growth in traditional society
- Stimulus needed to mobilize capital and resources
  - Revolution and institutional restructuring
  - Technological innovation
  - Favorable international environment
  - External Injection of capital
Stage 3: The Takeoff

- Productive investment must rise to 10 per cent of national income
- Needed: rapid accumulation of capital and productive investment
4. The Drive to Maturity

- Employment growth
- Growth in national income
- Rise of consumer demands
- Strong domestic markets
5. High Mass Consumption Society
The Importance of Capital Accumulation

• Capital accumulation is the name of the game
• So how does it happen?
Economic development and the International Economy

• International interdependence will lead to economic development of ALL countries in a liberal system

• Trade serves as an engine of growth
The Staples Theory

- Staples are field crops or minerals
- Earnings finance industrial growth
- Canada and Australia developed this way
- This justifies the theory of comparative advantage
- Export-led growth is the way to develop
Trade and the product cycle

• Corporations maximize their own growth and the growth of the countries in which they operate

• Three stages of corporate expansion and growth
the introductory or innovative phase

- Located in advanced countries
- Comparative advantage in product development because of large home market
- And lots of resources
- Corporation enjoys monopolistic position
- Foreign demand grows
- Corporation exports
The maturing phase of the product cycle

• Technology diffuses
• Innovative firm loses competitive edge as technology becomes available
• Advantage shifts to foreign production to replace exports and hold market share
• Innovative firm establishes foreign branches
The Standardized Phase

• Production fully routine
• Comparative advantage shifts to the developing country
• Export platforms develop
So....is there a symbiotic relationship between the MNC product cycle and global economic development?
As developing countries grow, they become sources of innovation.....
Research and Development

Asian Countries building their R&D Investments

Source: OECD Main Science and Technology Indicators. Compiled by the APS Washington Office.

Gross R&D as Percent of GDP

Japan, United States, Korea, Taiwan, Singapore, China

High Tech Exports

High-Tech Exports: U.S. Losing World Share

1980 $190 B*
- Emerging Asian Economies 7%
- Other 9%
- United States 30%
- Japan 13%
- European Union 41%

2003 $1,902 B*
- Emerging Asian Economies 26%
- Other 15%
- United States 16%
- European Union 32%
- Japan 9%

Source: National Science Foundation, Science and Engineering Indicators 2006, Appendix Table 6-4.
*1997 U.S. Dollars. Emerging Asian Economies: China South Korea, Taiwan, Singapore, Hong Kong, India. High-tech includes Aircraft, Pharmaceuticals, Office and computing machinery, Communication equipment, Medical, precision, and optical instruments, Communication equipment, Medical, precision, and optical instruments.
Role of International Institutions: conditions for loans and aid

• Internal liberalization of Markets
• Integration into the world Economy
• Reduction of extensive government programs because they .......
  – Tend of allocate funds to non-productive activities
  – Entrepreneurs can’t find funding
  – Create wrong incentives
  – Stimulate pressure for trade protection
So why do some countries stagnate and show little or no economic growth?

• External connections like trade and investment are important, but that’s not all.....

• There are internal requirements for development as well....
  – Overloaded bureaucracies and elite/military consumption, rent-seeking
  – Traditional culture must give way to modern culture....
<table>
<thead>
<tr>
<th>Tradition</th>
<th>Example</th>
<th>Modernity</th>
<th>example</th>
</tr>
</thead>
<tbody>
<tr>
<td>collective unit of social organization</td>
<td>Religion, ethnic group, tribe</td>
<td>Individual as the unit of social organization</td>
<td>U.S. Bill of Rights,</td>
</tr>
<tr>
<td>Personal ties govern social organization and behavior</td>
<td>family, tribe (feed corruption, suppress entrepreneurship)</td>
<td>Pragmatic and functional ties govern behavior</td>
<td>markets, professions, associations (feed merit and excellence)</td>
</tr>
<tr>
<td>essentialist Identity (one dimensional)</td>
<td>ethnic identity, religious identity, (us vs. them)</td>
<td>Multidimensional Individual identity</td>
<td>Example?</td>
</tr>
<tr>
<td>Identity derived from mystical principles</td>
<td>National identity (us vs. them)</td>
<td>Free choice of identity</td>
<td>See above (can conform to market signals)</td>
</tr>
<tr>
<td>Ascriptive hierarchies,</td>
<td>Kingdoms, families (rigidity)</td>
<td>Functional hierarchies</td>
<td>Parliaments, (flexibility, change)</td>
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Democracy and Markets

• Democracy and markets encourage each other: political and economic freedom are two sides of the same coin
## Summary of Liberal Theories of Development

<table>
<thead>
<tr>
<th>Stimulants</th>
<th>Internal</th>
<th>External</th>
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|            | • Human Capital  
|            | • Entrepreneurial Spirit  
|            | • Efficient Government  
|            | • Savings  
|            | • Research and Development  
|            | • Investments  
|            | = *Modern Society*  | • Opportunities to Catch Up  
|            |                       | • Foreign Investments  
|            |                       | • Trade  
|            |                       | • Aid  |
| Hindrances | • Political Instability  
|            | • Corruption  
|            | • Traditional Society  | • Trade Barriers in the North  
|            |                       | • Absence of project finance  
|            |                       | • Absence of Balance of Payments finance  |
Liberal perspective in a nutshell

- Economic growth is part of “modernization”
- Demography and Technology create conditions for growth
- Accumulation of capital
- Mass Consumer society