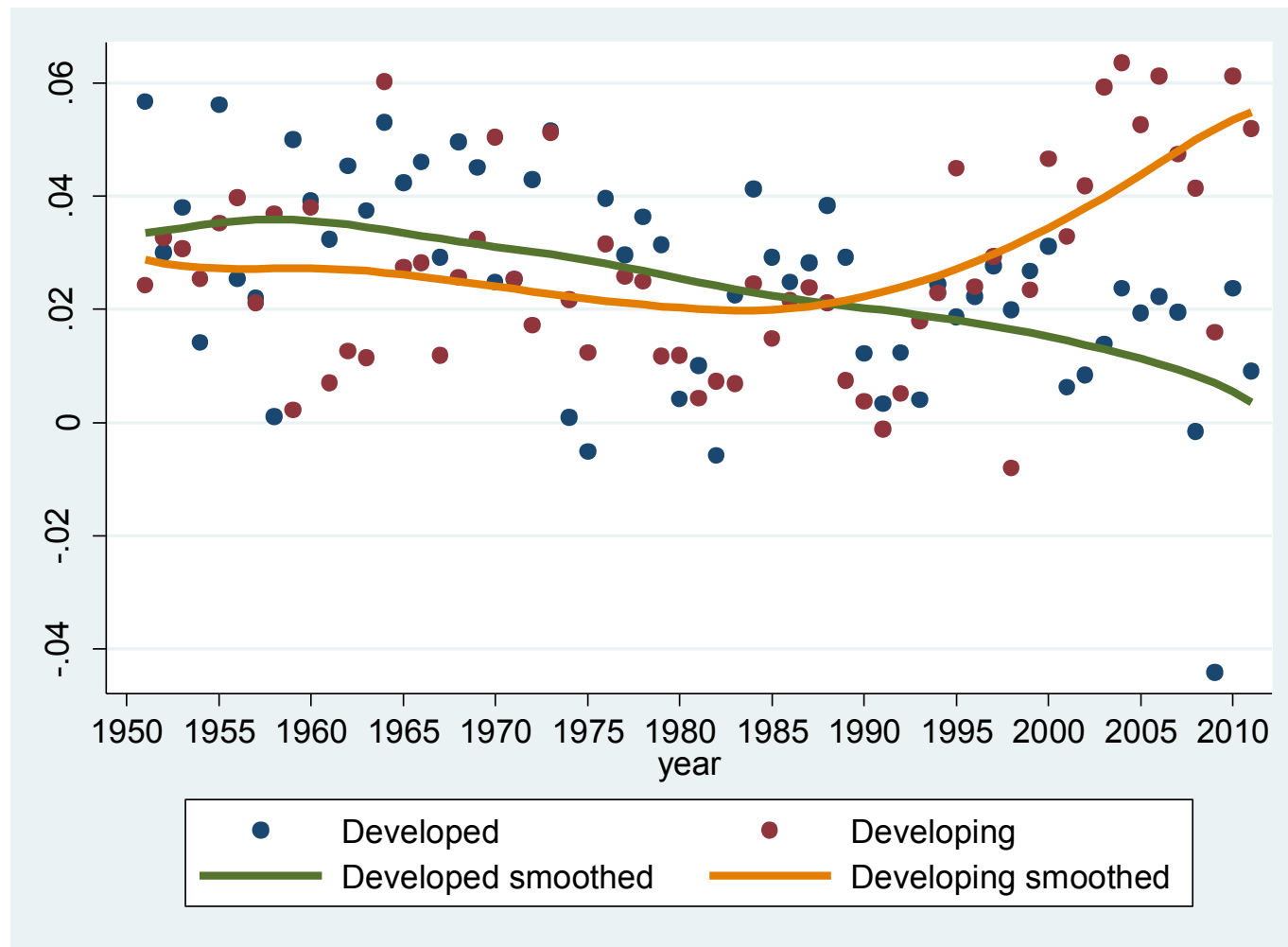


The Past, Present, and Future of Economic Growth

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Developing countries are now rapidly closing income gap with advanced countries



Growth trends in developed and developing countries, 1950-2011

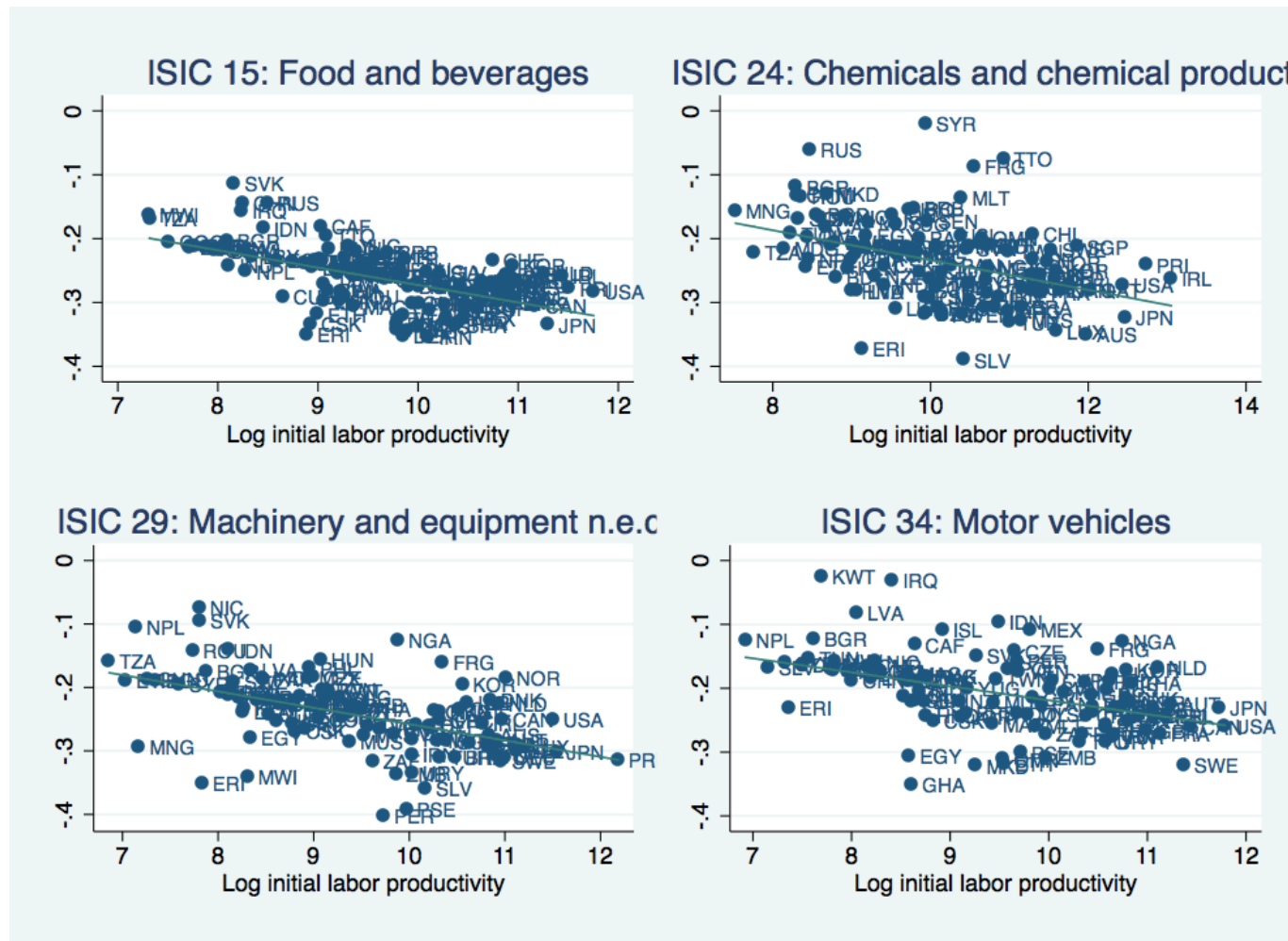
But will rapid convergence continue?

Understanding the mechanics of productivity growth:

- ▶ Escalator industries: exhibit unconditional convergence in productivity (manufacturing, tradable services?)
- ▶ Traditional industries: require steady investments in human capital and institutional capabilities



Manufacturing is archetypal escalator industry



Source: Rodrik (2012)

Notes: Vertical axis represents relative growth rate of labor productivity, controlling for period fixed effects. Each country enters with most recent decade for which data are available.

The two dynamics of growth

1. “Fundamentals”: building broad capabilities in the forms of human capital and strong institutions
 - ▶ Takes time, requires broad-based complementary investments, and produces steady but moderate growth
2. “Structural transformation”: emergence and expansion of modern (“escalator”) industries
 - ▶ Requires narrower range of reforms (that are often sectoral) to remove/compensate for costs modern industries face, and produces rapid growth until dualism eliminated

The set of policies required to foster these two dynamics overlap, but are not same

In particular, role of unconventional policies to stimulate new industries (as in East Asia)



A typology of growth outcomes (1)

		Structural transformation	
		<i>slow</i>	<i>rapid</i>
Investment in fundamentals	<i>low</i>	(1) no growth	(2) episodic growth
	<i>high</i>	(3) slow growth	(4) rapid, sustained growth



A typology of growth outcomes (2)

		Structural transformation	
		<i>slow</i>	<i>rapid</i>
Investment in fundamentals	<i>low</i>	(1) Sub-Saharan Africa	(2) Many countries under ISI, China?
	<i>high</i>	(3) post-1990 Latin America	(4) South Korea, Taiwan



The argument in brief

- ▶ Industrialization has been the route to rapid growth in the past
 - ▶ with manufacturing's ability to absorb low-skill labor a bonus from inclusion standpoint
- ▶ While steady accumulation of “capabilities” has been a requirement for longer-term convergence
- ▶ Industrialization has been typically promoted through pragmatic, opportunistic policies with “unorthodox” features
- ▶ A development-friendly global context has helped, through:
 - ▶ access to markets, capital and technologies of advanced countries
 - ▶ benign neglect towards structural transformation policies in developing countries



Prognosis

- ▶ Troubled times in advanced countries:
 - ▶ High public debt
 - ▶ Existential problems of the eurozone
 - ▶ Distributional struggles related to decline of middle class
- ▶ China's difficulties
- ▶ Less buoyant world economy
- ▶ Further pressures to narrow policy space in developing countries
- ▶ Reduced employment-absorption capacity of manufacturing
- ▶ The challenge of “green industries”



Policy

- ▶ Ultimately, economic performance will continue to depend mostly on what happens at home
- ▶ But policies will need to focus somewhat more on home markets and less on world markets
 - ▶ In particular, social and incomes policies that expand middle class and domestic market become more of a complement for growth policies
- ▶ Globally, need for a new settlement between advanced countries and large emerging markets
 - ▶ the latter can no longer be free-riders on the policies of the former
 - ▶ must moderate ambitions on financial globalization and regulatory harmonization to expand domestic policy space

