

Bringing Production Back into Development

- Keynote speech for the 2012
Development Studies Association (DSA)
Annual Conference

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Who are the entrepreneurs? – Proportion of self-employed people

Rich countries

- Average: 12.8%
- Norway: 6.7%
- US: 7.5%
- France: 8.6% (so, Dubya's comment was a classic case of the pot calling the kettle black)

Poor countries

- Average: 30-50%
- Ghana: 66.9%
- Bangladesh: 75.4%
- Benin: 88.7%
- Rich/Poor ratio: 2-4
- Bangladesh/US ratio: 10
- Norway/Benin ratio: 13

'Shocking ...
masterful'

OBSERVER

23
THINGS
THEY
DON'T
TELL
YOU
ABOUT
CAPITALISM



THE No.1 INTERNATIONAL BESTSELLER

Ha-Joon Chang



Development without Development: the MDGs

- Goal 1: Eradicate extreme poverty and hunger.
- Goal 2: Achieve universal primary education.
- Goal 3: Promote gender equality and empower women.
- Goal 4: Reduce child mortality.
- Goal 5: Improve maternal health.
- Goal 6: Combat HIV/AIDS, malaria, and other diseases
- Goal 7: Ensure environmental sustainability.
- Goal 8: Develop a global partnership for development.

Neglect of Production I – Neo-Liberalism

- Neoclassical economics that provides the main economic arguments for neo-liberalism is basically about market exchange and has little to say about production.
- In the neo-liberal discourse, the issues surrounding the development of productive capabilities is assumed away, as it takes capabilities as given and focus on incentives.
- Believing in the power of the free market, the neo-liberal discourse criticizes any attempt to deliberately enhance productive capabilities through public policy intervention as being at best futile and at worst counter-productive.

Neglect of Production II – Humanism

- Since the 1980s, there has been a ‘humanist’ reaction against what was seen as the collectivist, materialistic biases of the early development discourse.
 - The early development theories were mainly about transforming the productive structure through policies affecting aggregate variables, like savings, investments, and surplus labour.
 - In applying these theories, individuals were forgotten and, worse, repressed in the name of the greater good, called economic development.
- This has made the ‘humanists’ emphasise the need to enhance individual capabilities through health, education, and empowerment, as reflected in the MDGs and the conditional cash transfer programmes.

Neglect of Production III – Post-Industrialism

- According to the discourse on post-industrial service economy, rising income has brought about the shift of demand towards services.
- They cite cases like Switzerland and Singapore as examples of service-based prosperity.
- The issue of productive development is almost completely ignored in this discourse, as it is implicitly assumed that even the poorest countries possess the capability to compete in services.
 - The recent Indian success story with services is presented as the proof of this.

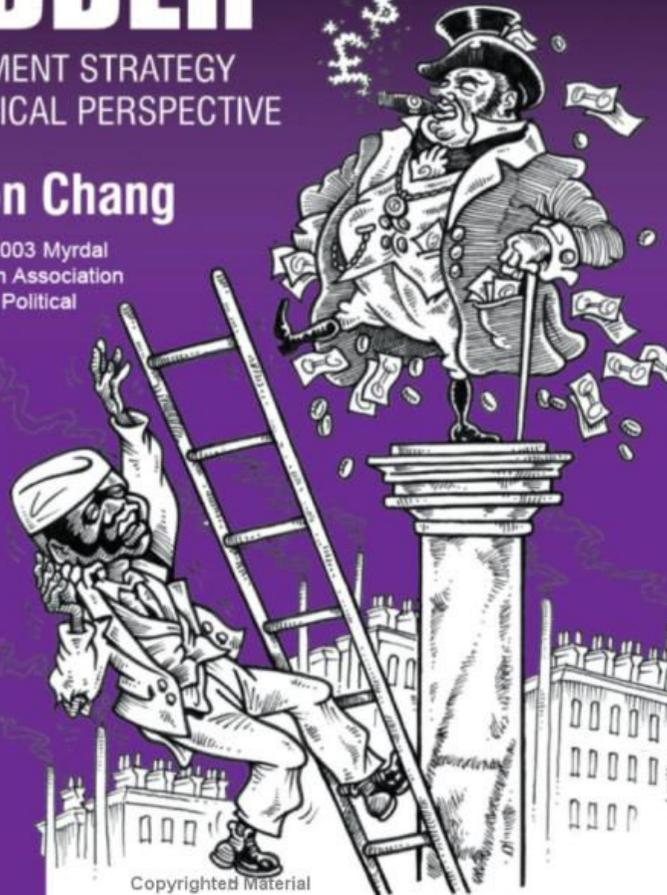
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KICKING AWAY THE LADDER

DEVELOPMENT STRATEGY
IN HISTORICAL PERSPECTIVE

Ha-Joon Chang

Winner of the 2003 Myrdal
Prize, European Association
of Evolutionary Political
Economy



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'Probably the world's most
effective critic of globalization'
MARTIN WOLF, *FINANCIAL TIMES*

'Lucid, deeply informed'
NOAM CHOMSKY



BAD SAMARITANS

**THE GUILTY SECRETS
OF RICH NATIONS
& THE THREAT TO
GLOBAL PROSPERITY**

HA-JOON CHANG

Theoretical justifications for policies increasing productive capabilities through public intervention

- the infant industry argument
- various Neoclassical theories of market failure, especially those related to knowledge generation and the capital market
- the Big Push argument
- Hirschman's linkages theory
- Arrow's theory of learning-by-doing
- neo-Schumpeterian arguments on National Systems of Innovation
- even the Austrian theory of tacit knowledge may be re-formulated to justify industrial policy, especially in relation to developing countries

Why it is not enough to enhance individual capabilities to raise a society's productive capabilities

- Developments in productive capabilities mainly occur inside productive enterprises, rather than at the individual level.
 - 1,000 street food stalls or 1,000 one-man TV repair shops vs. one modern supermarket or one electronics manufacturer, each employing 600 workers and getting supplied by 20 small enterprises that employ 20 people each on average.
 - Boeings and Volkswagens as what distinguish the US and Germany from Nigeria and the Philippines
- In addition to business enterprises, enhancing a society's productive capabilities requires a series of collective institutions that encourage and help different economic actors work together – capital-labour collaboration within firms, cooperation among firms within and across sectors, government-business interaction (including, but not just, industrial policy), industry-academia partnership, etc..

Problems with the Post-Industrial Economy Discourse

- The increasing share of services does not mean that material production is not important any more.
 - We are in fact consuming an ever-increasing amount of material goods.
 - The rise in the share of services happens mainly because services are becoming relatively more expensive, given the faster rise of productivity in the manufacturing sector.
- A lot of recent productivity growth in service sectors like finance and retail has been illusory.
 - The high productivity growth of the financial sector turned out to be based on dubious asset valuation and has come at a huge costs to the rest of the economy.
 - A lot of the increases in retail service productivity in countries like the US and Britain have been bought by lowering the quality of the retail service itself – fewer sales assistants, longer drives to the supermarket, lengthier waits for deliveries, etc..
- Most high-value services – finance, engineering, IT services, consulting, etc. – mainly sell to the manufacturing sector, so they cannot prosper without a strong manufacturing base.



“In Italy for thirty years under the Borgias, they had warfare, terror, murder, bloodshed, but they produced Michelangelo, Leonardo da Vinci and the Renaissance. In Switzerland, they had brotherly love - they had five hundred years of democracy and peace, and what did that produce? The cuckoo clock.”

**(Orson Welles as Harry Lime,
The Third Man)**

Wrong, wrong, wrong, wrong, wrong!

- Five hundred years of democracy?
 - Women were given votes only in 1971.
 - Two rogue cantons refused to give women votes until 1989 and 1991.
- Five hundred years of peace?
 - Wars with Swabia (1499) and France (1515 and 1798)
- Five hundred years of brotherly love?
 - Civil wars in 1653, 1656, 1712, and 1847
- The cuckoo clock was *not* invented in Switzerland.
 - It was invented in Germany.
- Switzerland is *not* an economy living off the black money deposited by Third World dictators and selling cuckoo clocks and cow bells to American and Japanese tourists (or, if you want to be nice to it, a post-industrial economy relying on services like banking and tourism).
- It is one of the most industrialised economies in the world.

Manufacturing Value Added Per Capita, 2005

(in constant 2000 US dollars; index USA=100)

- Japan: \$8,474 153
- **Switzerland:** \$6,874 124
- **Singapore:** \$6,708 121
- Sweden: \$6,462 117
- Finland: \$5,939 107
- USA: \$5,528 100
- Luxembourg: \$4,496 81
- Korea: \$3,827 69
- UK: \$3,707 67
- Mexico: \$1,001 18
- Brazil: \$749 14
- China: \$496 8
- India: \$83 1.5

Source: UNIDO, *Industrial Development Report, 2009*

How about India?

- The truth is that India's service trade has *not* been much of a success
 - Until 2004, India had deficit in service trade.
 - Between 2004 and 2009, India recorded service trade surplus equivalent to 0.9% of GDP, which covered only 19% of its manufacturing trade deficit (4.8% of GDP).
- This means that, unless it increases its service trade surplus by 5 times (an implausible scenario, given that its service trade surplus has *not* even been on a firm rising trend since 2004), India cannot maintain its current pace of economic development without a serious balance of payments problem.

Negative Consequences of Neglecting Production I

- Even while producing more was emphasized, how to increase the capabilities to produce was not taken seriously.
- This has made a lot of people think that what countries produce to earn income does not matter – “It doesn’t matter whether you produce potato chips or micro-chips”, to borrow a famous expression from the 1980s industrial policy debate in the US.
- This has, in turn, made a lot of developing countries complacent about their dependence on commodities or cheap assembly.
- However, in the long run, different economic activities give different scope for growth and technological development, so even from a purely growth-oriented point of view, this line of thinking is problematic.

Negative Consequences of Neglecting Production II, III, & IV

- The neglect of productive capabilities has also meant that our assessment for policies have acquired short-term biases.
 - Policies that reduce current consumption with a view to increasing long-term productive capabilities, such as infant industry protection or deliberate increase in investments, were too easily dismissed.
- In particular, the collective dimensions of productive development were neglected, making people ignore the issues of how to develop modern firms and other institutions that are central to productive development.
 - There is of course a lot of talk of ‘private sector development’ but it is mainly a ‘negative’ agenda in the sense that deregulation and cutting taxes are seen as the key to enterprise development.
- The neglect of production has also led to a very partial view of our individual well-being.
 - Envisaging people as consumers rather than producers, issues of employment, the quality of jobs, and workplace welfare have been ignored.

Reconstructing the Development Discourse – Bringing Production Back In

- We need to reconstruct our development discourse by bringing production back in.
- This is not to suggest that we go back to the older aggregate approach solely focused on resource mobilization and labour absorption.
- This reconstruction has to be done by combining those old insights with the more recent theoretical developments on technological learning, technological innovation, and enterprise development.
- It also has to take individuals seriously – not just as consumers (as in neo-liberal economics) nor just as citizens with entitlements (as in the humanist approach) but also as producers, who have to worry about employment and the contents of their work.

More information

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