

Developmentalism at the Periphery: Can productive change and income distribution be compatible with global financial asymmetries?

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Starting point

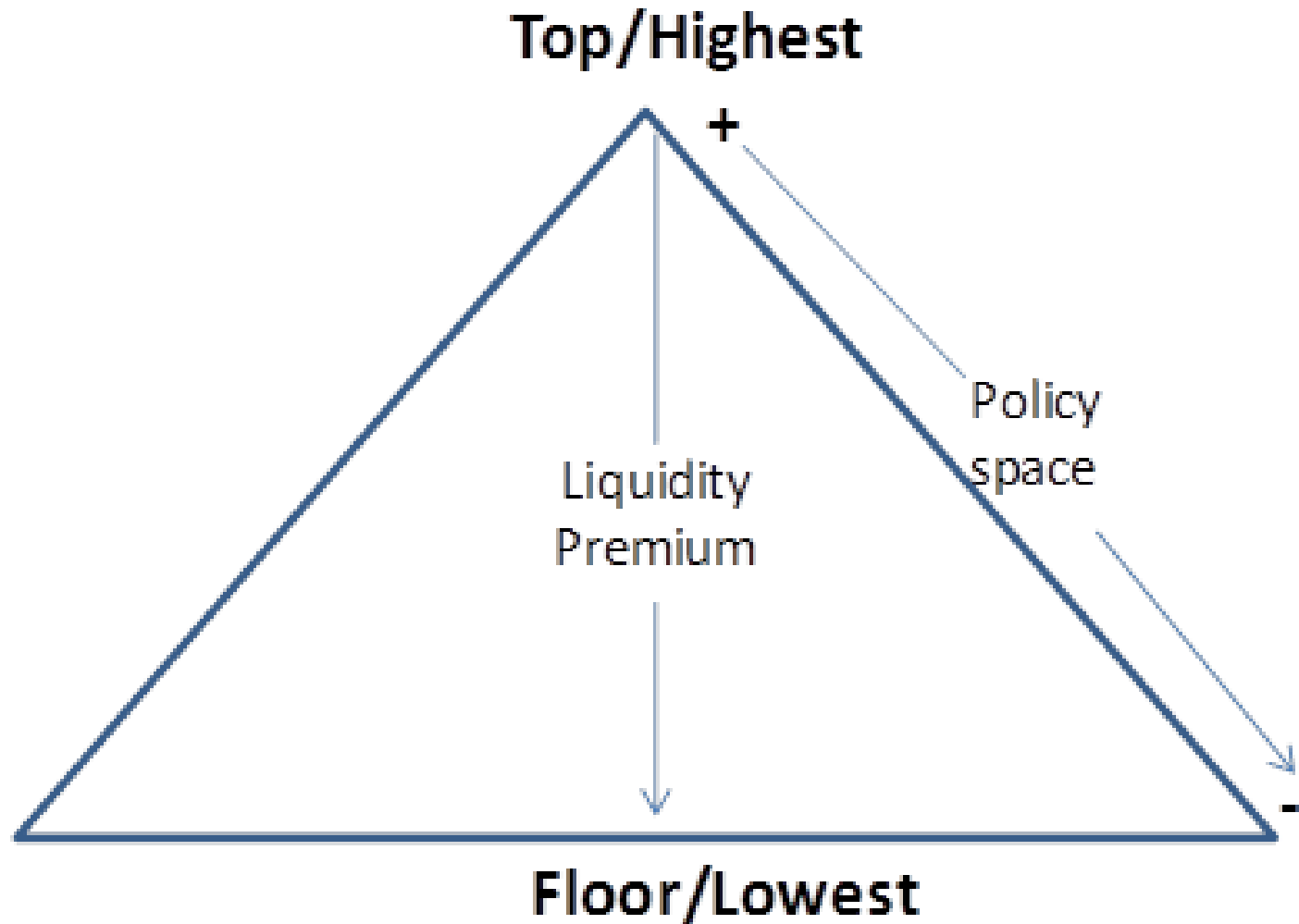
- Latin America: after poor economic performance in the 1980s and 1990s, GDP grew 4.1% in 2004-2013 compared to 2.7% in 1984-2003, but with recent slowing down.
- At the same time, some improvement in terms of equity, and reduction of poverty.
- The profound discontent with “Washington Consensus” style policies opened the discussion about the use of more active state public policies.
- New strategies of developmentalism emerged in Latin America in the 2000s and 2010s: (i) new developmentalism; and (ii) social developmentalism
- Also, there is some recent literature that shows that financial globalization and global currency hierarchy have reduced policy space for domestic purposes in emerging economies.

Questions

- How does asymmetrical monetary system impose policy constraints to developmentalist strategies in their different modalities?
- What sort of macroeconomic policy agenda for a developmentalist strategy would be required in order to deal with this sort of policy constraints?
- Do such developmentalist strategies incorporate redistributive policies in a functional way for sustained growth and productive change?

- ✓ International monetary system is seen as hierarchical and asymmetric institutional arrangement organized around a hegemonic currency, with a privileged position in the monetary hierarchy (pound sterling, US dollar)
- ✓ Investors concentrate their portfolios in key currencies (US dollar, Euro, Yen, etc.) with higher liquidity premium
- ✓ “Currency Hierarchy”:
 - ✓ Below the key-currency (US dollar), currencies issued by other centre developed economies
 - ✓ At the bottom, currencies issued by peripheral emergent economies, that have to compensate low liquidity premium of their currencies with high returns (domestic interest rate, currency overvaluation).

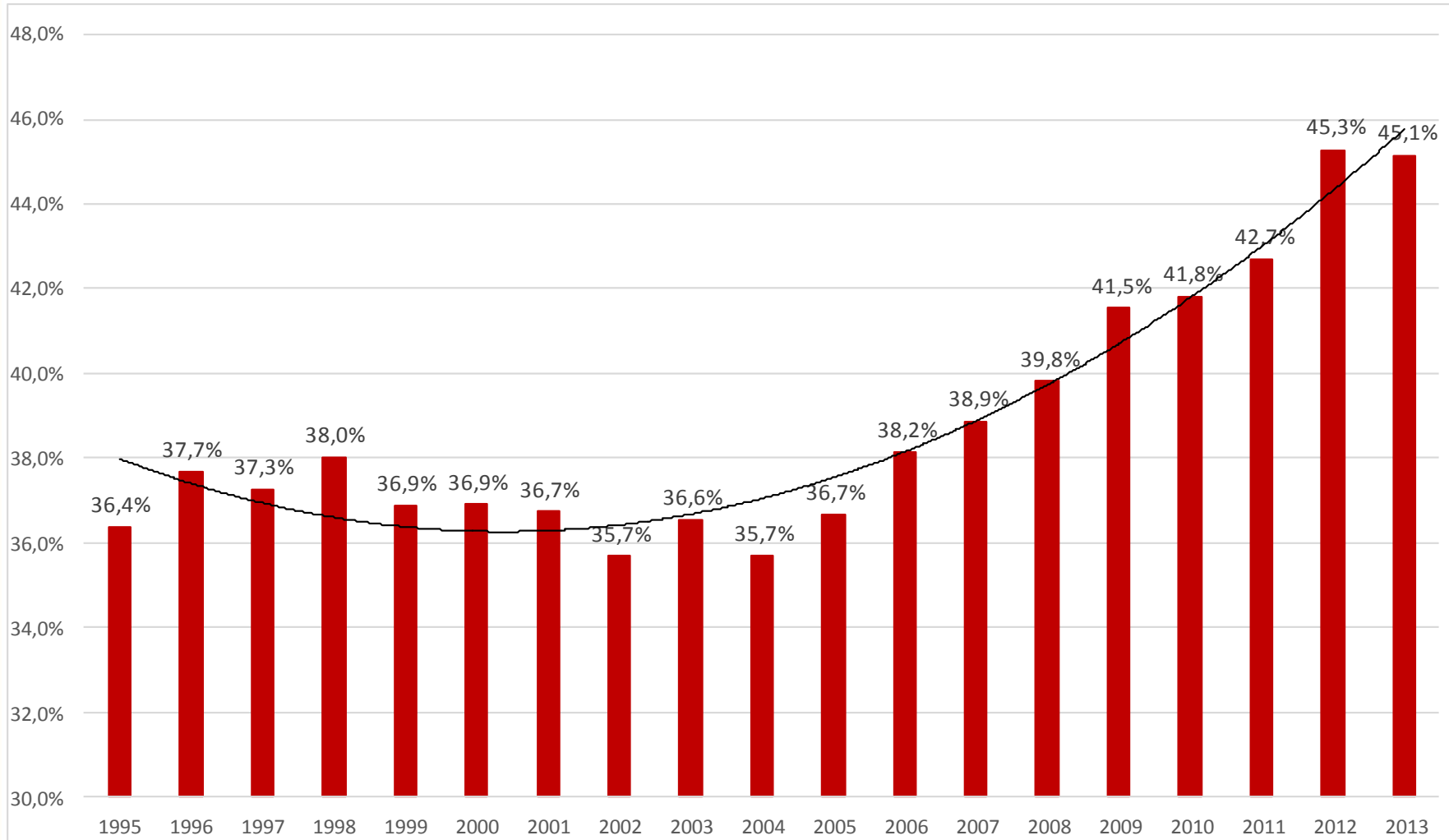
Currency hierarchy or currency pyramid



New concepts of developmentalism

- Developmentalism is defined by Fonseca (2014) as an imprecise term that includes project of economic development; structural change (industrialization); and active role of the state.
- In contrast to “Washington Consensus”- type policies
- but also differing from classical developmentalism (CEPAL)
 - less direct state intervention; more concern about price stability
 - redistribution via social policies
- Two main concepts of neo-developmentalism emerged:
 - a. ‘New developmentalism’ (Bresser et al.)
 - b. ‘Social developmentalism’ (Bastos 2012; Bielschowsky 2012; Carneiro 2012)
- **Background:** Brazil’s economic and social policy of the 2000s as emblematic case of growth with some redistribution

Wage Share in Brazil (salary mass over GDP – 2012 prices)



New-developmentalism:

- Two fundamental macroeconomic problems in middle-income countries: (i) *tendency of wages to increase below the productivity rate*, in consequence of the availability of unlimited supply of labor; and (ii) *tendency towards currency overvaluation* (combination of ‘Dutch disease’ in commodity exporters economies plus abundance of net foreign capital flows).
- Implementation of an *income policy* that keeps wages growing in line with productivity, and an *exchange rate policy* that counteracts the tendency to currency overvaluation and that has as target an ‘*industrial equilibrium exchange rate*’ - that is, a rate that enables producers of state-of-the-art manufactured goods to compete in foreign markets with a fair profit margin (Bresser-Pereira 2011)
- According to this strategy, a developing economy must resort to an *export-led strategy* for a short period of time when the current growth rate is growing below the rate needed to perform the catching-up.

Social-developmentalism:

- Economic growth should be driven by the *domestic mass market*, “which will be the more the better is the income distribution” and also by “favorable outlook for public and private demand for investments in (economic and social) infrastructure” (Bielschowsky 2012, p. 730).
- In particular, the growth of the ‘domestic mass market’ should be stimulated both by the expansion of employment and improvement in the income distribution as a result of *redistributive governmental policies* (increase of minimum wage, and expansion of social spending) and *stimulus to consumer credit*.
- Secondly, as a growth strategy based on mass consumption might lose momentum with the passage of time, the expansion would have to be completed by *autonomous investment*, i.e. by public investment in economic and social infrastructure (Carneiro 2012, p. 775).

- Comparison:

	Social developmentalism	New developmentalism
Aims	Productive change with broad income redistribution Industrialization pushed by domestic market growth	Productive change with moderate income redistribution Re-industrialization
Targets	Increase of domestic market (consumption) Improvement in income distribution Balanced trade account	Trade balance surplus (manufacturing net exports) Moderate improvement in income distribution
Tools	Public investment Active industrial policies Wage policies (i.e. real increase in minimum wage) Social policies (income transfers) Active fiscal policies Financing of development: consumer credit; active role of public banks	Competitive exchange rate Capital account regulation Limiting external debt Industrial policy for export promotion Moderate trade liberalization Wage policy (real increase in minimum wage along with productivity) Long-term fiscal equilibrium with some room for counter-cyclical policies

Both approaches with merits and limits

- 'New developmentalism': virtuous cycle by competitive exchange rate
 - fulfills necessary condition for currency at lower end of hierarchy
 - Some concern about implementation of a export-led growth in democratic societies
 - negligence with long-term financing mechanisms
 - but sufficient for income redistribution?
- 'Social developmentalism': virtuous cycle by income redistribution
 - Some negligence with macroeconomic consistency and some inclination towards appreciated exchange rate
 - risk to be overthrown by returning balance of payment constraint
 - social policies subordinated to fostering mass consumption

Developmentalism under constraints of currency hierarchy

How can developmentalist combine reducing macroeconomic volatility, reducing inequality, and structural change?

Proposed combination:

- “Modern protectionism” with regulation of capital flows
- Priority for a stable and competitive exchange rate
- Foster domestic financial development (low interest rate, stimulus to long-term public debt, strategic role of public banks)
- Use of fiscal and wage policies to support inflation stabilization
- Industrial policy well coordinated with macroeconomic policy
- Social policies to reduce volatility, operating as automatic stabilizers
 - unemployment insurance
 - progressive income taxes (income –related taxes, taxation of capital income and wealth)

- No easy task!
- Enormous effort to create conditions to enlarge “policy space” in emerging economies
- Global coordination problem: not all countries can have export surplus at the same time
- But feasible, depending also on correlation of forces