

Overview

Analytical Framework & Transformation Strategy



Policy Formulation in Developing Countries

About This Course

- ❑ How development policies are designed and implemented (HOW rather than WHAT).
- ❑ Methodology: comparison of international best and worst practice cases (not mathematical modeling or cross-country regressions).
- ❑ We will look at both *positive* and *normative* aspects (how things are and how things should be).
- ❑ We will deepen our knowledge without necessarily arriving at one conclusion.
- ❑ Interactive and open-ended discussion, with students presentations toward the end

Today's Topics:

Background Ideas for Policy Formulation

- Politics and economics
- Key relationships that determine policy effectiveness
- Policy learning
- Institutional dynamics
- Middle income traps
- Comparing policy quality

Creation of a Developmental State

Predatory/patrimonial state—power and state machinery for perpetuating personal benefits of leader, his family and friends

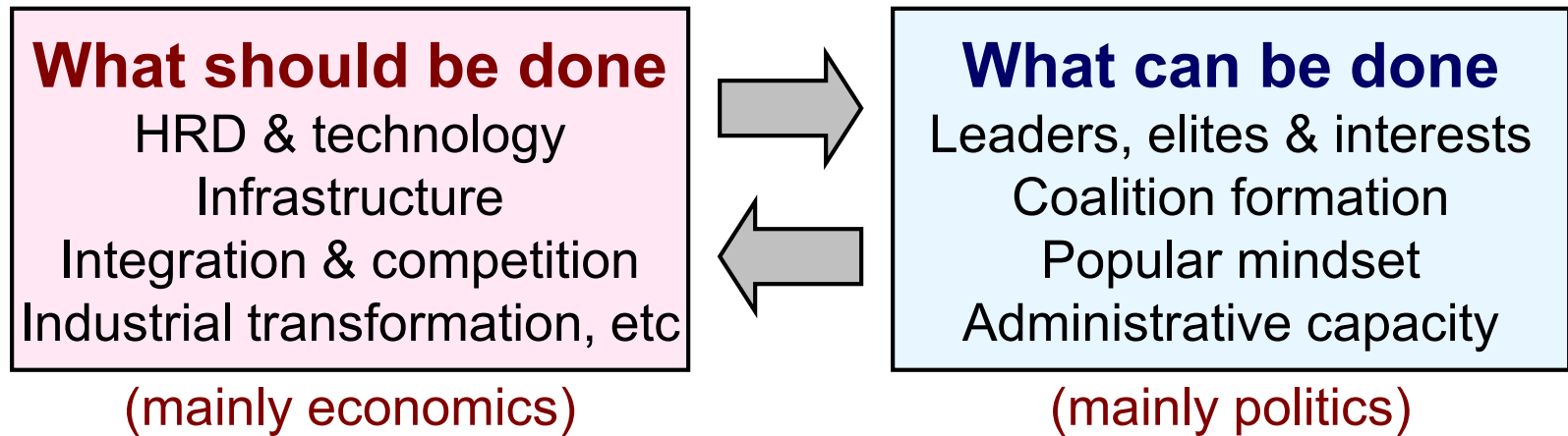
Developmental state—policies and institutions for value creation and competitiveness for all people and enterprises

How can we promote DS instead of PS?

- Political approach—encourage/fight for the emergence of developmental leaders and agenda
- Donors' approach—support leaders and groups that are developmental and action-oriented
- Academic approach—show concrete and feasible growth models for willing governments to learn and adopt

Policy: Desirability vs. Feasibility

Development is both a political process and an economic process.



- ❑ Each country is unique in *what needs to be done* (economics) as well as *what can actually be done* (politics & administrative capacity).
- ❑ Any policy maker must work with economic and political space simultaneously.

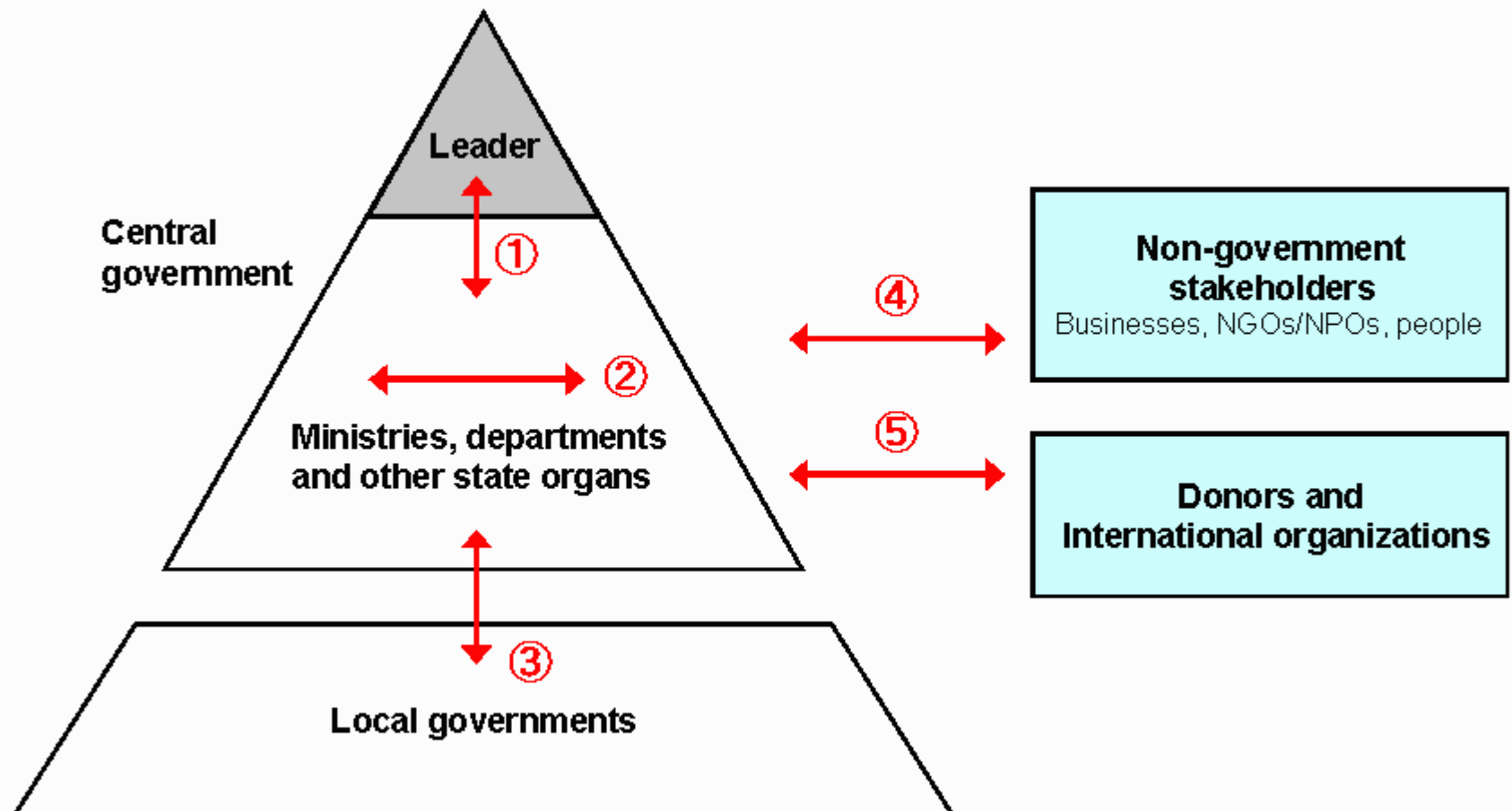
Key Relations and Coalitions

1. Leadership style
2. Horizontal coordination within central government
3. Vertical coordination between central and local governments
4. Relation with non-government stakeholders
5. Relation with foreign players

We look at these five relations which are critical in determining policy effectiveness.

We do not pre-impose one ideal form (“international best practice”) on each relation. Answers may be many. Each country must devise its own based on local reality.

Key Relations and Coalitions



Learning from Other Countries

- ❑ To improve policy, a comparative perspective is crucial across countries, across time, and across sectors and firms.
- ❑ Learn **mindset** and **methodology** for conducting industrial strategies effectively. Learn *how to make policies*.
- ❑ Early achievers (Japan, Korea, Singapore, etc.) improvised policies through self-effort and trial-and-error. For today's latecomers, more systematic learning is possible and perhaps desirable.

What must be Learned?

- ❑ Policy measures (WHAT)
- ❑ Policy procedure and organization
- ❑ Policy structure—vision, strategy, action plans, monitoring, etc.
- ❑ National movement for mindset change
- ❑ Making of a developmental state (under democracy)
- ❑ Transition from developmentalism to advanced society

The key is to acquire **capability to create policy packages suitable for each country and situation** using foreign models as building blocks.

Government can learn by self-study or with help from advanced countries (policy dialogue).



K. Ohno, *Learning to Industrialize*, Routledge, 2012 (Open Access)

Distinguishing Common and Unique Features

- ❑ In any international comparison, universal features and country-specific features are always present. Clearly distinguish them when deciding what to import from abroad.
- ❑ It is necessary to (i) select the right benchmark countries and periods (not any model); and (ii) properly adjust foreign models to suit your local context.
- ❑ Two attitudes that fail:
 - (i) Refusal to learn from others (“we are very unique, and other countries cannot be our model.”)
 - (ii) The copy-and-paste approach (a good model should be adopted regardless of the conditions of the home country).

Confucius (551-479BC): 「子曰学而不思則罔思而不学則殆」 “Learning without thinking is useless; thinking without learning is precarious.”

Learning = knowledge collection

Thinking = creation of your model by selection and adjustment

Institutional Dynamics

After understanding the current status and setting the desired goal, how can we move from the one to the other?

Common obstacles:

- Political resistance: corruption, vested interests, neo-patrimonialism, predatory state
- Incompetence: leaders, advisors and officials do not know or care
- Lack of knowledge or a mistake in designing transition steps
- Bureaucratic sectionalism: no ministry or department has full authority or responsibility to execute reform; inertia or rivalry prevails

Comparative Institutional Analysis

- Prof. Aoki and others at Stanford University and Tokyo University initiated CIA.
- It is based on evolutionary game theory
- Some questions
 - ✓ Why do multiple systems emerge and coexist, without any system dominating all others?
 - ✓ What is the dynamic mechanism of moving from one system to another?



Masahiko Aoki
1938-2015

Key Concepts of CIA

Institutional complementarity

Many institutional elements are complementary and reinforce each other (e.g., OJT, life-time employment, keiretsu system, main banks, management-labor cooperation, etc. in Postwar Japan)

Strategic complementarity

Individuals adopt strategies that fit particular social rules (e.g., people in competitive society study professional skills; people in connection society give parties & gifts)

Path dependence

Any system, once started, will persist unless enormous effort or shock impacts it (e.g., continuation of the US system, Japanese system, Chinese system, etc. with only minor changes)

Forces of Systemic Change

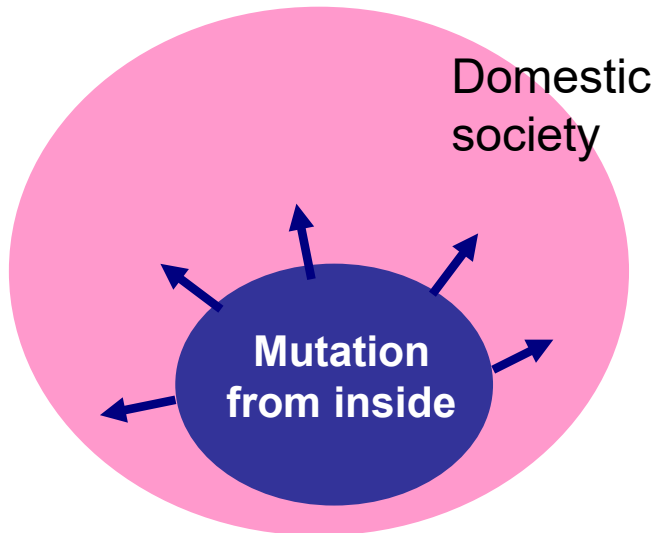
How can a solidified social system change?

- ❑ Collective mutation
- ❑ Foreign pressure (contact with another system)
- ❑ Policy as *deus ex machina*
 - Strong leader
 - Political parties, interest groups, people's movement
 - Researchers, advisors, intellectuals

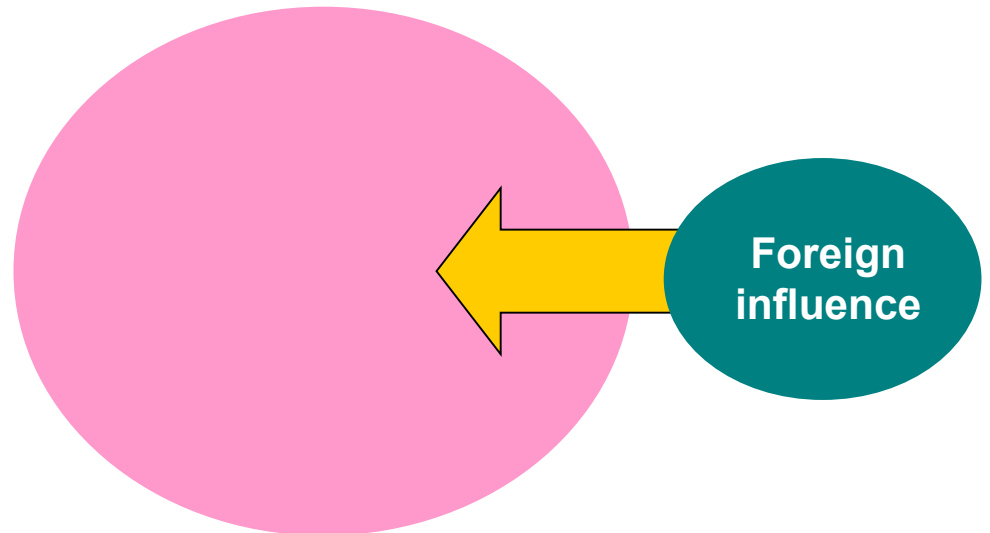
Those who are inside the country but do not follow the rules of the existing system initiate change against resistance

- ❑ Combining policy and foreign pressure

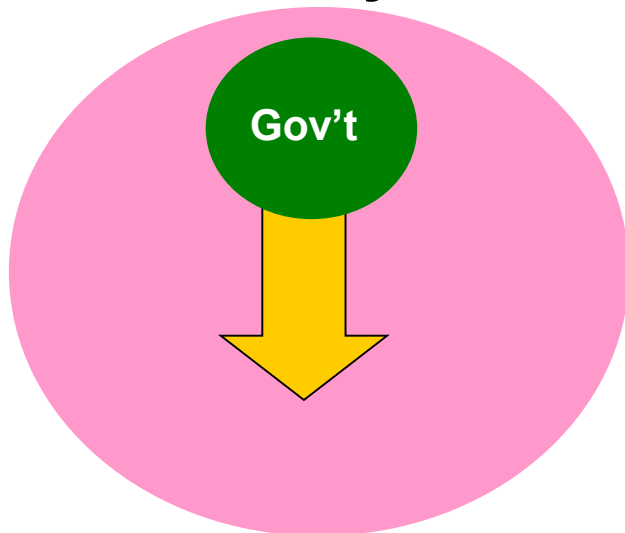
Collective mutation



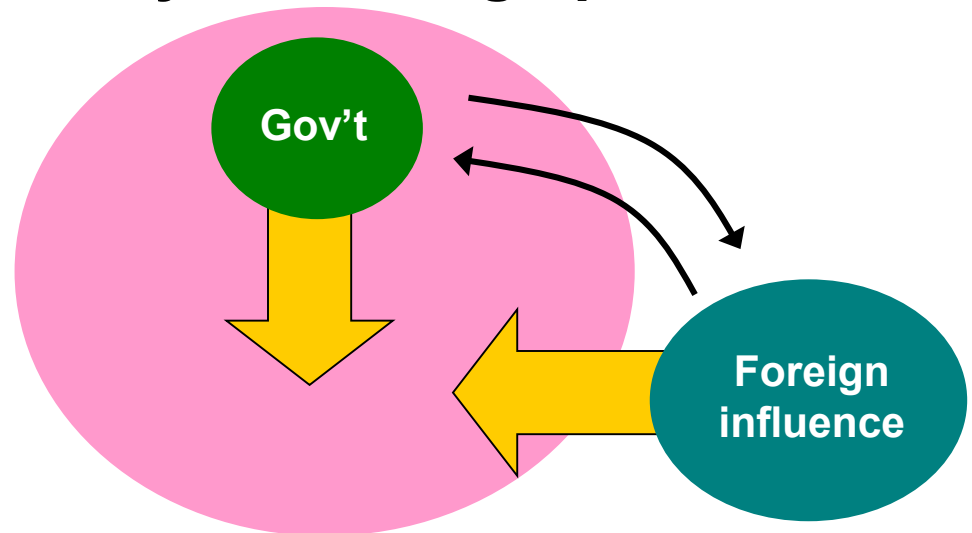
Foreign pressure



Policy



Policy and foreign pressure



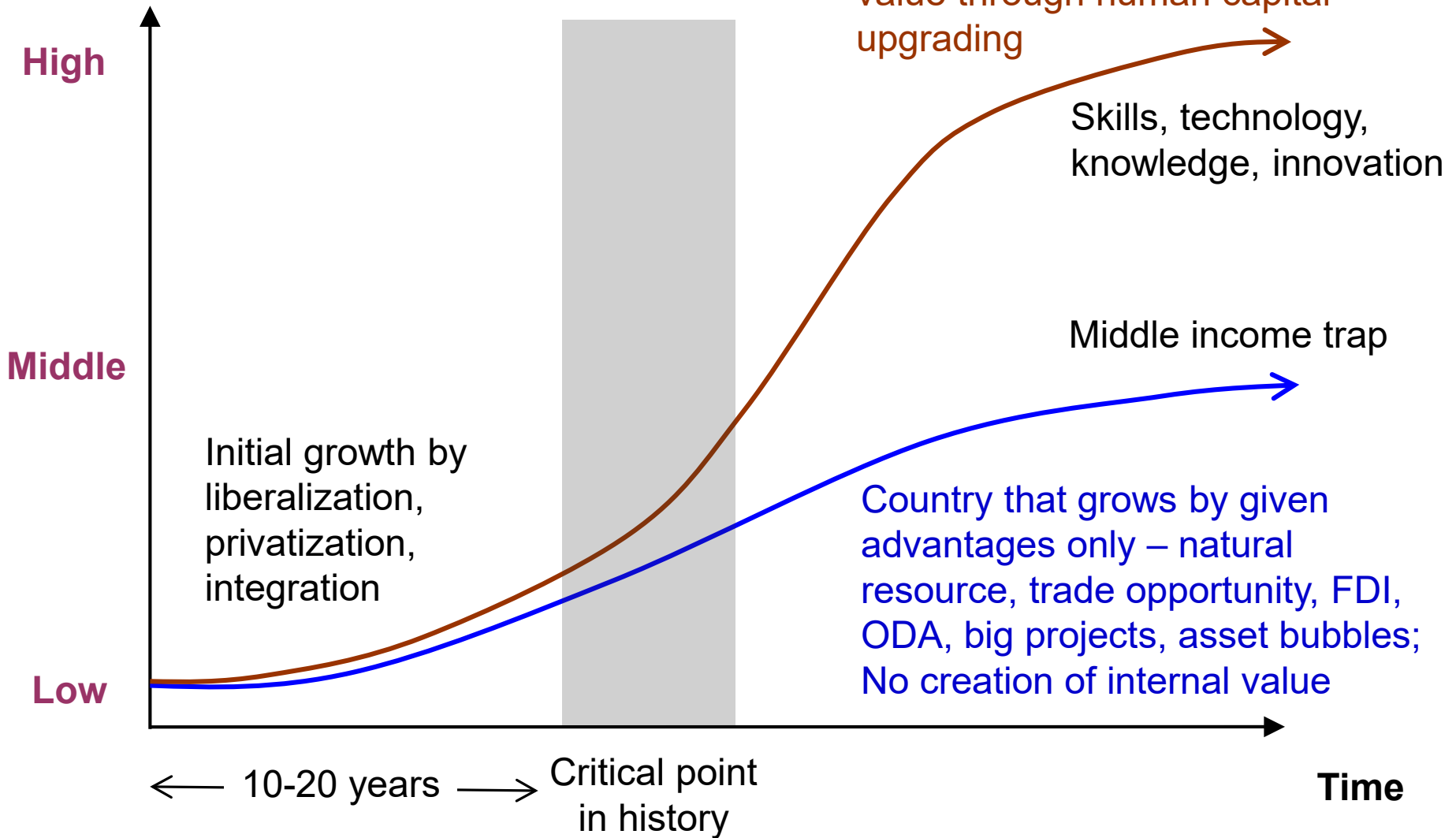
Middle Income Traps

A Structural Definition

- ❑ A middle income trap is the situation where an economy is stuck at income dictated by given resources and initial advantages, and cannot rise beyond that level (*growth is given, not created*).
- ❑ Countries may reach middle income by liberalization, privatization and integration, but reaching higher income requires strong policy effort to promote private dynamism, not laissez-faire.
- ❑ Growth based on FDI, aid, big projects, natural resources, or locational advantages will eventually end. The true source of development is value creation by domestic citizens and enterprises.

Why Do Countries Diverge?

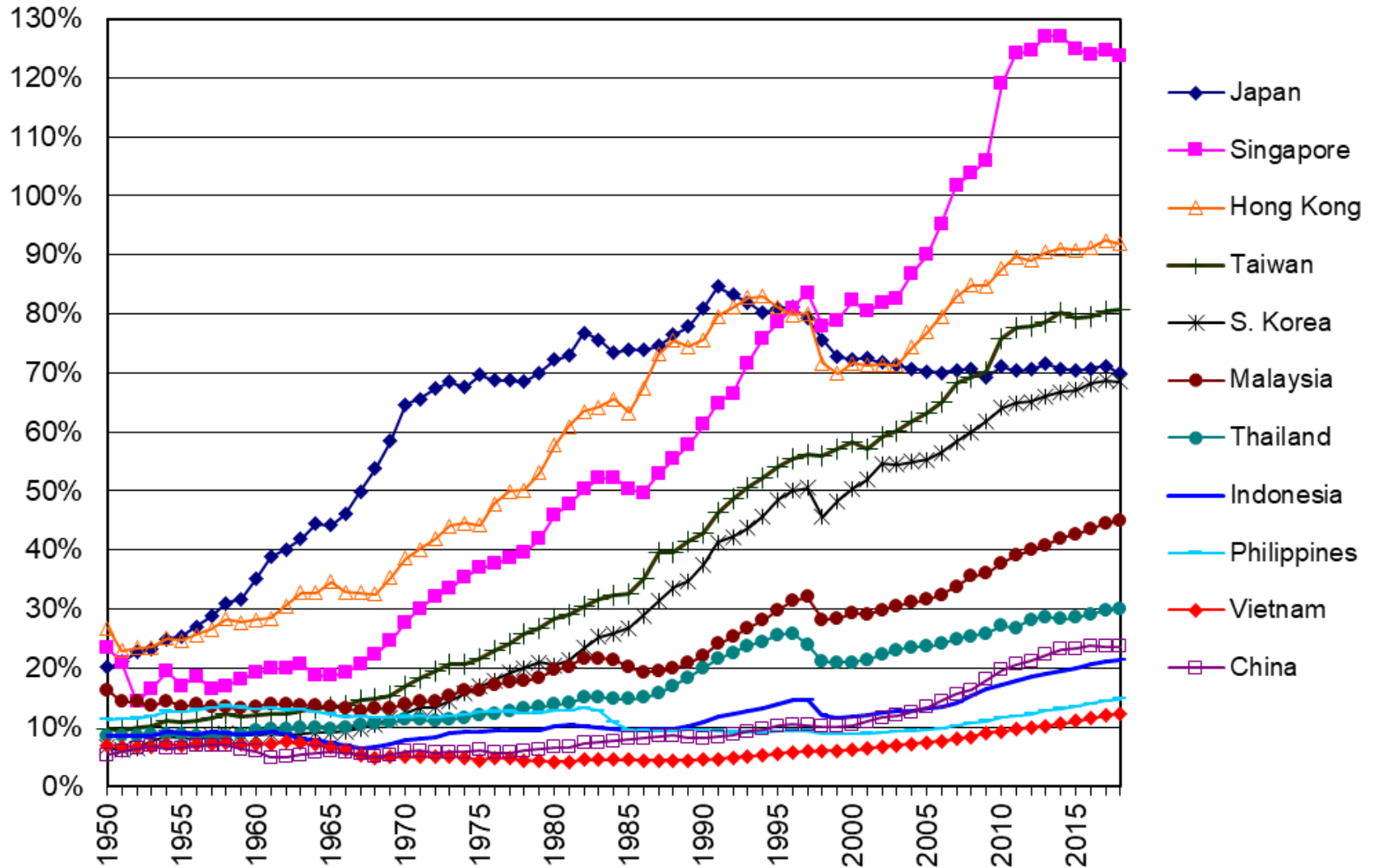
Per capita income



Speed of Catching Up: East Asia

Per capita real income relative to US

(Based on Real GDP per capita in 2011USD)

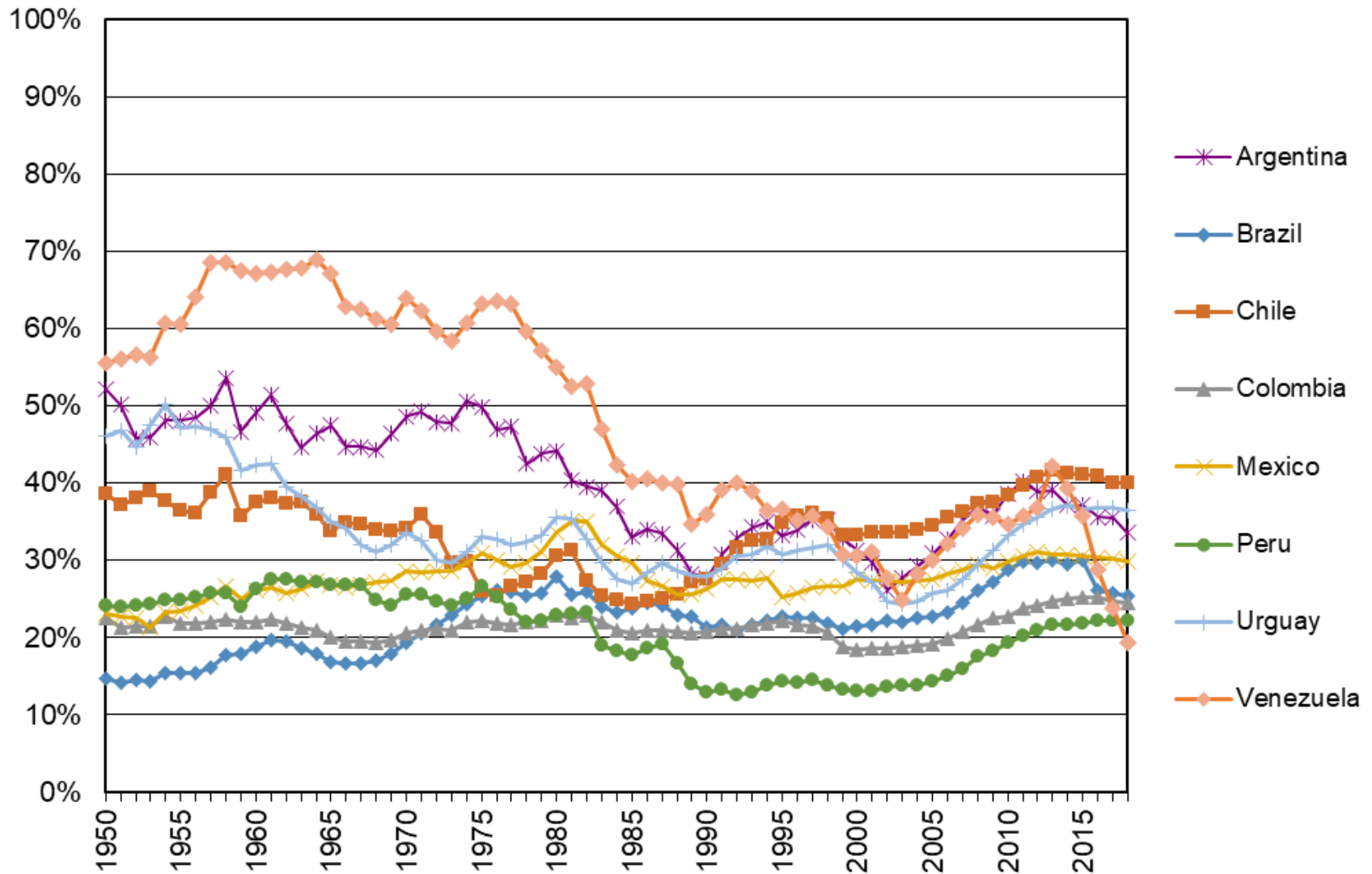


Source: Maddison Project Database, accessed on April 8, 2021.

Latin America

Per capita real income relative to US

(Based on Real GDP per capita in 2011USD)

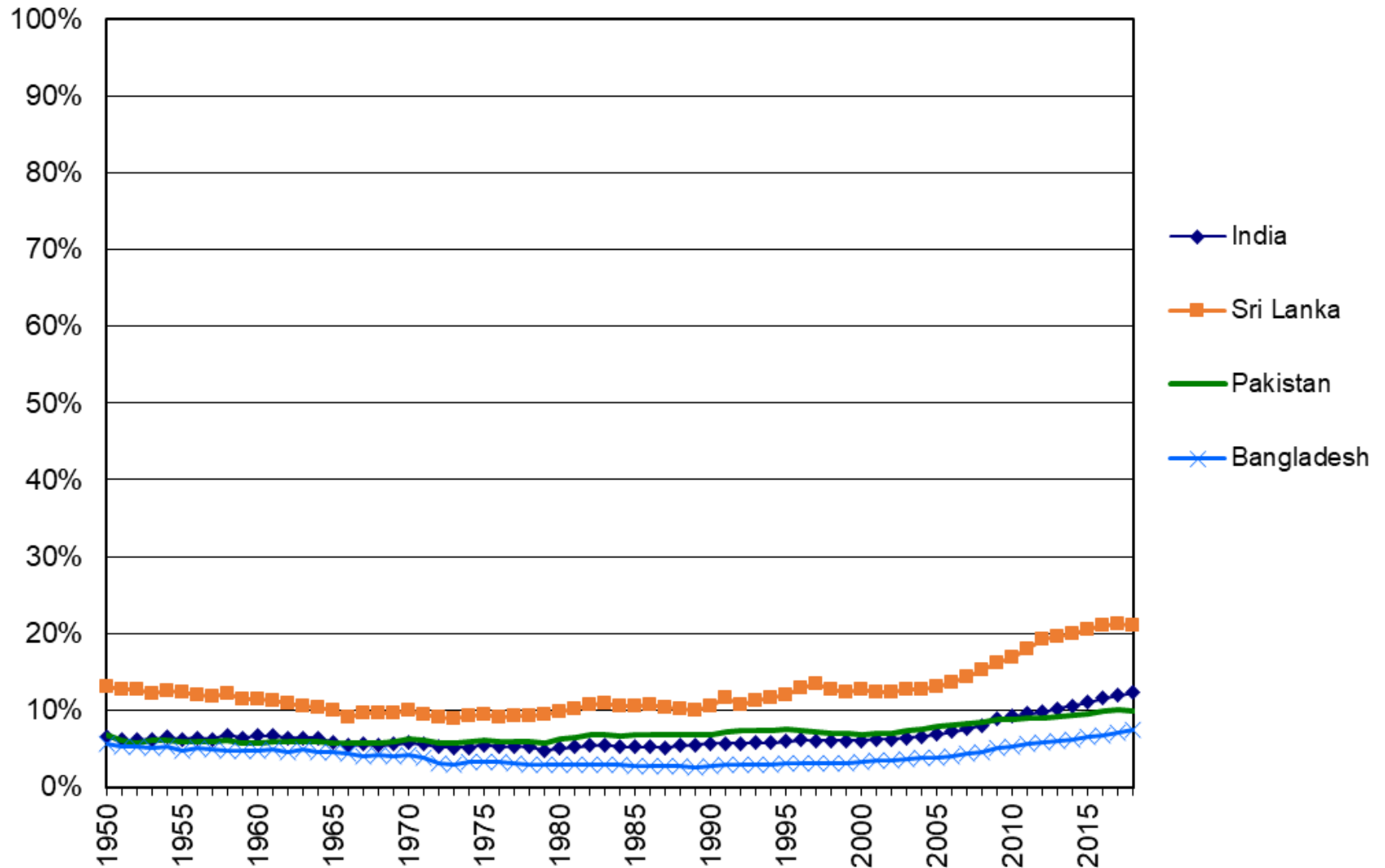


Source: Maddison Project Database, accessed on April 8, 2021.

South Asia

Per capita real income relative to US

(Based on Real GDP per capita in 2011USD)

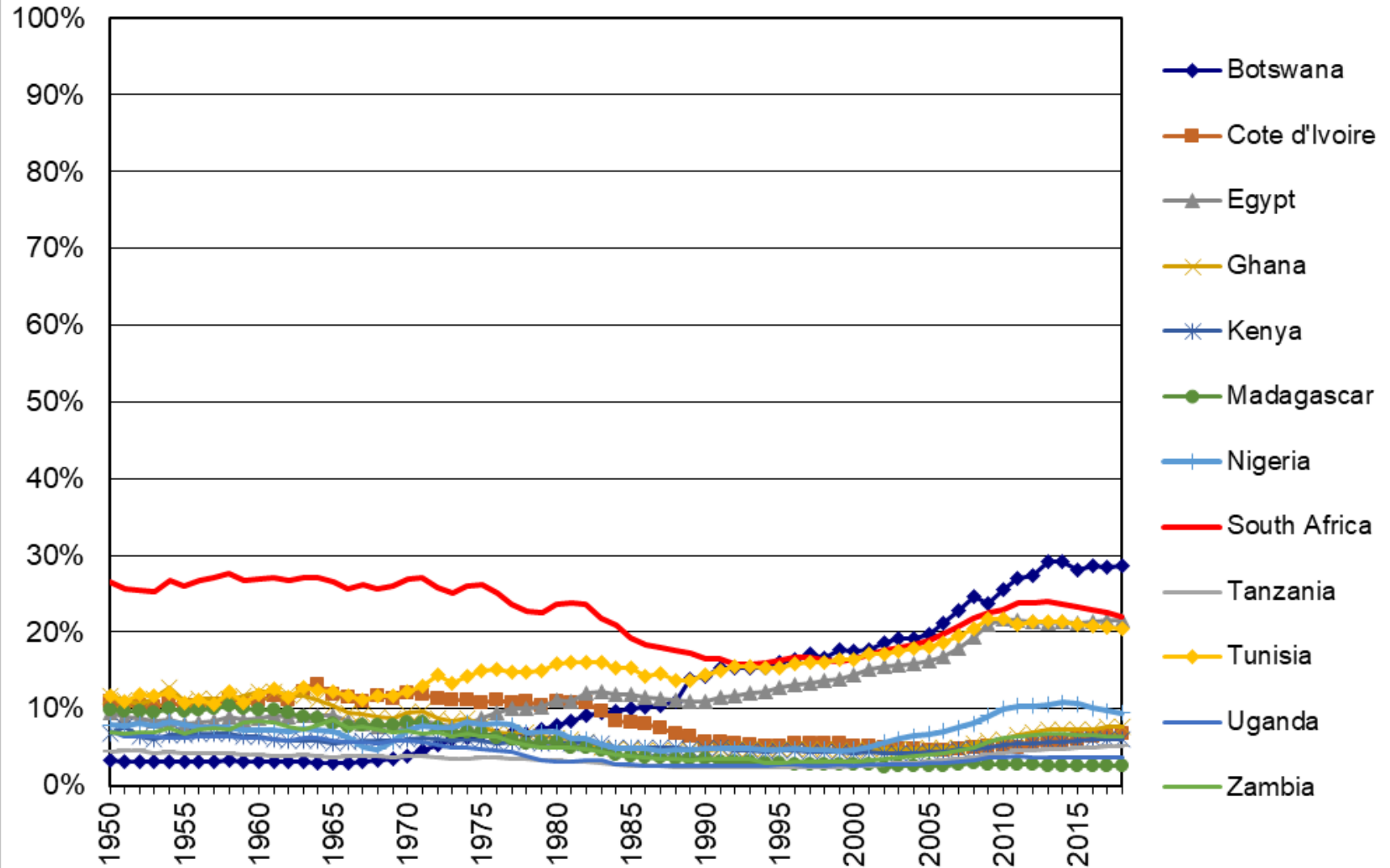


Source: Maddison Project Database, accessed on April 8, 2021.

Africa

Per capita real income relative to US

(Based on Real GDP per capita in 2011USD)

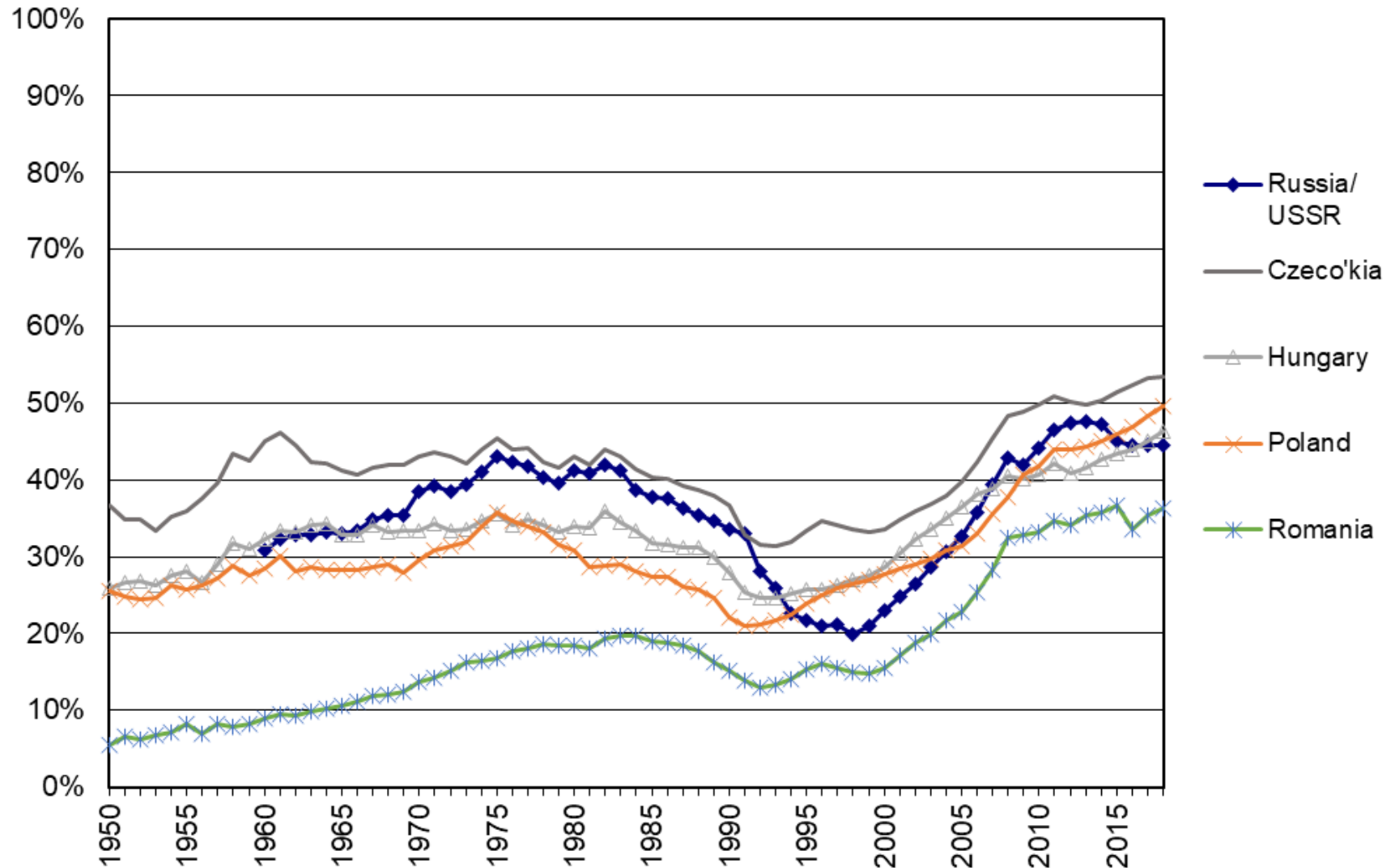


Source: Maddison Project Database, accessed on April 8, 2021.

Russia & Eastern Europe

Per capita real income relative to US

(Based on Real GDP per capita in 2011USD)



Source: Maddison Project Database, accessed on April 8, 2021.

Policy Quality Matters

- ❑ Development performance differs greatly across nations. Some nations quickly reach high income while others slow down or stagnate at low or middle income.

**Economic performance = Private dynamism + Policy quality
+ External factors**

- ❑ Government must learn and improve policy making in order to support private dynamism and cope with external shocks. This requires serious policy learning.
- ❑ Long-term economic performance depends less on initial conditions (poverty, colonialism, conflicts, etc.) and more on policy quality.

Quality of Industrial Policy vs. Income

(preliminary results)

	Date of research	Evaluation of industrial policy sub-components										Average	Grade	For reference only	
		Industrial human resource	Domestic enterprise development	Business climate	Power and logistics	Export promotion	Strategic FDI marketing	Industrial parks	Supporting industries & FDI-local firm linkage	Productivity, technology & innovation	Standards and testing			Per capita income (WB, 2013, USD)	Doing Business ranking (WB, 2014, among 189 entries)
Singapore	Aug.-Sep. 2010	5	4	5	5	4	5	5	4	5	5	4.7	A +	\$55,183	1
Japan	Continuous	5	5	4	5	4	3	3	...	4	5	4.2	A	\$46,330	29
Korea	Nov. 2010	5	4	4	5	5	3	4	...	4	5	4.3	A	\$25,977	5
Taiwan	Mar. 2011	5	5	5	5	3	4	5	...	5	5	4.7	A +	\$22,597	19
Malaysia	2006, 2010, 2013	3	4	4	5	4	5	4	1	4	4	3.8	B	\$10,538	18
Mauritius	Oct. 2012	4	4	4	4	4	5	4	3	4	3	3.9	B	\$9,478	28
Thailand	2005, 2009, 2013, 2015	3	2	4	4	3	4	4	4	2	4	3.4	B	\$5,779	26
Indonesia	Jun. 2014	2	2	2	2	2	3	1	1	1	2	1.8	D	\$3,475	114
Vietnam	Continuous since 1995	1.5	1.8	2.0	2.8	1.6	1.7	2.2	1.5	1.4	1.5	1.8	D	\$1,910	78
India	Sep. 2012	1	1	1	2	3	1	2	1	1	1	1.4	D	\$1,498	142
Cambodia	May 2015	0	1	4	3	1	2	3	0	0	1	1.5	D	\$950	135
Rwanda	Aug. 2014	2	2	4	3	3	4	4	2	2	1	2.7	C	\$639	46
Ethiopia	Continuous since 2008	3.0	1.9	1.7	3.1	3.9	4.3	4.4	2.0	3.2	2.0	3.0	B -	\$505	132

Notes:

1/ Evaluation: 0 (non-existent or worse), 1 (little), 2 (some), 3 (moderate), 4 (good), 5 (excellent). For Vietnam and Ethiopia, for which detailed data are available, points are given to the first decimal point.

2/ Letter grades: A+ (4.5 or above), A (<4.5), B (<4), C (<3), D (<2), F (<1).

3/ Evaluation of policy prepared and implemented by national government only; results obtained by private effort, international cooperation, or external conditions are excluded.

4/ It is somewhat difficult to evaluate the policy of a mature economy, such as Japan and Korea, with a large number of industrial policy measures in the past and at present. Grades may differ depending on which measures are evaluated and how much weight is given to past achievements relative to present policies.

Source: K. Ohno, "The Quality of Industrial Policy as a Determinant of Middle Income Traps," paper presented at Singapore Economic Review Conference, Singapore, August 2015.

Industrial Policy Quality: Summary

	Industrial policy quality		Per capita income (WB, 2013, USD)	Doing Business ranking among 189 entities (WB, 2014)
	Mean	SD		
Singapore	4.70	0.48	\$55,183	1
Japan	4.22	0.83	\$46,330	29
Korea	4.33	0.71	\$25,977	5
Taiwan	4.67	0.71	\$22,597	19
Malaysia	3.80	1.14	\$10,538	18
Mauritius	3.90	0.57	\$9,478	28
Thailand	3.40	0.84	\$5,779	26
Indonesia	1.80	0.63	\$3,475	114
Vietnam	1.80	0.43	\$1,910	78
India	1.40	0.70	\$1,498	142
Cambodia	1.50	1.43	\$950	135
Rwanda	2.70	1.06	\$639	46
Ethiopia	2.95	1.02	\$505	132

Log of per capita income

