Transforming an Economy: Challenges and Lessons for Namibia

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Major changes in development thinking in the last fifteen years

• Broader goals
  • Not just growth, but sustainable, inclusive, and democratic growth

• More instruments and policy frameworks
  • Industrial policies can work
  • New instruments in old areas: macro-prudential regulation
  • New tools: Conditional Cash Transfers; Micro-credit
  • Better management of natural resources: better auctions, better contracts
Major changes in development thinking in the last fifteen years

- New actors
  - Now recognize importance of civil society
  - The provision of the public good is a public good, and will normally be “undersupplied”
- New development banks
- A variety of institutional arrangements
  - Not just for-profit institutions and government
    - In US, some of the most successful institutions are not-for-profit foundations (e.g. universities)
  - Many examples of successful cooperatives

Cont’d
Major changes in development thinking in the last fifteen years

• New thinking
  • The only sustainable growth is inclusive growth: equality and growth are complements
  • Rents are pervasive in the economy—the competitive model does not describe well a modern economy
    • Who captures rents, what limits rents, how the rents are used becomes critical

Cont’d
Major changes in development thinking in the last fifteen years

• Neoliberalism has become thoroughly discredited
  • Led to more instability, lower growth, and more inequality
    • Structural adjustment programs in Africa led to lower growth and deindustrialization
  • Even the IMF has argued for the importance of equality
  • Even the IMF has argued for the use, at times, of capital controls
  • Privatizations have often failed
• But the legacies are still with us
  • Trade and investment agreements
  • Eurozone constructed on its principles is a failure, and is dragging down global growth

Cont’d
Major changes in development thinking in the last fifteen years

- New challenges and opportunities
  - Slowdown in global growth in 2015 is likely to continue
  - Slowdown in China is central
    - Contributing to end of commodity price boom
  - Most countries have not been able to offset forces leading to more inequality

Cont’d
Major changes in development thinking in the last fifteen years

- In US, recovery likely to continue to be anemic
  - Capping a third of a century of neoliberal policies—leading to median income lower than a quarter century ago, median income of a full time male worker lower than four decades ago, and wages at the bottom the same as sixty years ago—a failed economy
- Eurozone stagnation likely to continue
  - Crisis is not over
  - Flawed at birth—based on flawed economic models

Cont’d
Major changes in development thinking in the last fifteen years

- Export led growth model may be over
  - Global manufacturing employment in decline
  - Fight for share of that declining employment
  - Will have to be shift to services
  - Services are less traded
- New technologies have opened up new opportunities
  - Especially important in communication

Cont’d
Explaining shift in development thinking

- Influenced by major successes and failures of the last 30 years
  - Which have also led to reshaping our understanding of development
- Development/growth beyond anything that had been thought possible
  - And contrary to what others (Myrdal) had thought would occur
- The success of East Asia, including China
  - Hundred of millions moved out of poverty
- Based on government assuming a major role in the economy
  - But using markets
Explaining shift in development thinking

- Major debate about what it was that the government did that led to success
  - Different countries did different things, policies changed over time
- Also influenced by successes and failures elsewhere
  - Success of micro-credit schemes
  - Failures of most of transitions to market economy
  - 2008 crisis showed dangers of excessive deregulation

Cont’d
Explaining shift in development thinking

- Benefits of growth do not automatically get shared
  - Trickle down economics doesn’t work
    - US prime example
- Similarly situated countries can have markedly different outcomes
  - Inequality in US much larger than in other advanced countries
    - Without any offsetting benefits, e.g. in growth
  - In some countries, inequality is even going down—inequality is not just a matter of economics

Cont’d
Explaining shift in development thinking

• Inequality is a choice
  • A result of our policies, our rules, how we design institutions, what we spend money on, etc.
• That means politics matters—economics and politics inseparable
• Economic inequality gets translated into political inequality, which leads to more economic inequality in a vicious circle

Cont’d
Explaining shift in development thinking

- Influenced by major changes in economic theory and research
- New insights into failures of markets
  - Theories of imperfect and asymmetric information
  - Game theory/imperfect information
- Behavioral economics
  - Model of “rationality” underlying most economics flawed
- Important implications
- Policies can change beliefs, perceptions (central message of World Development Report of 2015)

Cont’d
Metrics

- Metrics have become increasingly important, but wrong to focus narrowly on GDP
- The International Commission on The Measurement of Economic Performance and Social Progress emphasized deficiencies in measure
  - (a) what we measure affects what we do and the design of policy: metrics are important;
  - (b) no single number can capture something as complex as our society;
  - (c) accordingly, there will have to be a “dashboard of indicators;”
  - (d) the dashboard which is appropriate for one country may be different from that of another;
  - (e) but among the metrics that should be included are those that reflect distribution and environmental sustainability;
  - (f) there needs to be improvements in the way we measure the value of government and other services;
  - (g) median income adjusted for inflation almost certainly reflects a better measure of what is happening to the typical individual, and therefore it should be among the numbers
Structural transformation

- All countries are in need of structural transformation
  - In advanced countries, in response to technology and globalization
    - From manufacturing to service sector
  - In China, from export led growth to domestic demand driven growth
    - From quantity to quality
  - In all countries—in response to need to address problems of climate change (both mitigation and adaptation)
  - In natural resource economies—to diversify away from dependence on natural resources
Structural transformation

- Markets on their own don’t manage these transformations well
  - Impediments imposed by capital market imperfections
  - Important externalities and coordination failures
- Government needs to assume an important role
  - Industrial policies are major tool

Cont’d
Industrial policies

- Central to economic/structural transformation
  - Key failure of many resource based economies was not to diversify during commodity price boom
  - Justified in terms of standard theories of market failures—instances in which markets on their own do not produce efficient outcomes
  - Affecting the structure of production and the choice of technology
- Broad objectives (not just GDP: environment, equality, employment, economic diversification)
Among key challenges facing Namibia

• Diversifying economy
• Achieving inclusion
• Addressing climate change
• Increasing employment
• Promoting growth
• Some of these are complementary, in other cases there may be trade-offs
• Will require *multiple* strategies
  • Some focusing on employment creation, some on inclusion, some on achieving a modern, diversified economy
Industrial policies

- Especially important in creating a learning society/knowledge economy—
  - Real source of wealth of economy
  - Especially important in 21st century
- Focus on knowledge spillovers/learning-by-doing effects
- Many instruments
  - Competitive and Stable Real Exchange Rates
  - In many countries, development banks have played an important role
    - May be especially important in lending to SME’s, as a source of “venture capital”
- Need a development oriented intellectual property regime
- Agenda entails strengthening the public sector and enhancing its capabilities
Industrial policies

- Every country has an industrial policy
  - Embedded in expenditure and tax policies, and basic legal framework
  - Some countries do not realize that they have an industrial policy
    - US policy: promote dysfunctional financial sector
    - Worked: sector grew enormously
Special opportunities and challenges of small open economies

Challenges

• Can’t avail themselves of economies of scale
  
  • Therefore, more exposed to risk of monopolies, imperfections of competition, less able to adequately diversify
  
  • Markets will underestimate macro-economic benefits of diversification
  
  • Implication: greater need for competition policies and industrial policies to promote diversification
  
• More subject to being buffeted by global risks—but more need to remain open
  
  • Implication: need to have better systems of sharing—sharing risks and benefits of openness
  
• One of major insights of Scandinavian countries
Special opportunities and challenges of small open economies

Some advantages

• One can develop a small niche and be successful
  • Finland illustrates

• One may be able to achieve broader societal consensus, without the large divides so frequently exhibited in large countries
  • May not happen automatically

• One may more easily be able to detect abuses of market and government power
  • Information asymmetries may be less
  • Again: this doesn’t happen automatically, need appropriate institutions and laws
A word about natural resource economies

Present special problems

• Have been less successful than one might have expected: the natural resource curse

• Lower growth, more inequality

  • A result of failure to manage volatility, high exchange rates that disadvantage other exports and import competing sectors, and rent-seeking

  • Not inevitable: some countries have managed resources well, investing proceeds in people, infrastructure, establishing stabilization funds, managing exchange rates, diversifying economy

  • If proceeds are not re-invested, country is poorer (wealth below ground is diminished, while wealth above ground not increased commensurately)

• Another example where GDP is not a good measure
Managing natural resource wealth

• Wealth belongs to the country as a whole, should be managed for the benefit of the country as a whole

• Good, well-designed auctions can maximize the value of the proceeds going to nation as a whole

• Good, well-designed contracts can provide good incentives, balancing risk sharing
  • Fundamental conflict between private sector and government
    • Private sector wants to minimize what it pays government, maximize government assumption of risk

• Transparency rules help ensure that the country gets full benefit and proceeds are well spent

• Wealth of experience of bad practices
Concluding comments

- Namibia has been relatively successful in its growth
  - But has not done so well in achieving shared prosperity
  - With high unemployment, high Gini coefficient
- Namibia has the potential for performing still better
  - Taking better advantage of its resources
  - Better diversifying its economy
  - And taking on board the important lessons of development of the last third of a century