

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

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

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

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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

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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

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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

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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

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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

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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)

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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

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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