WORLD ECONOMICS INTRO

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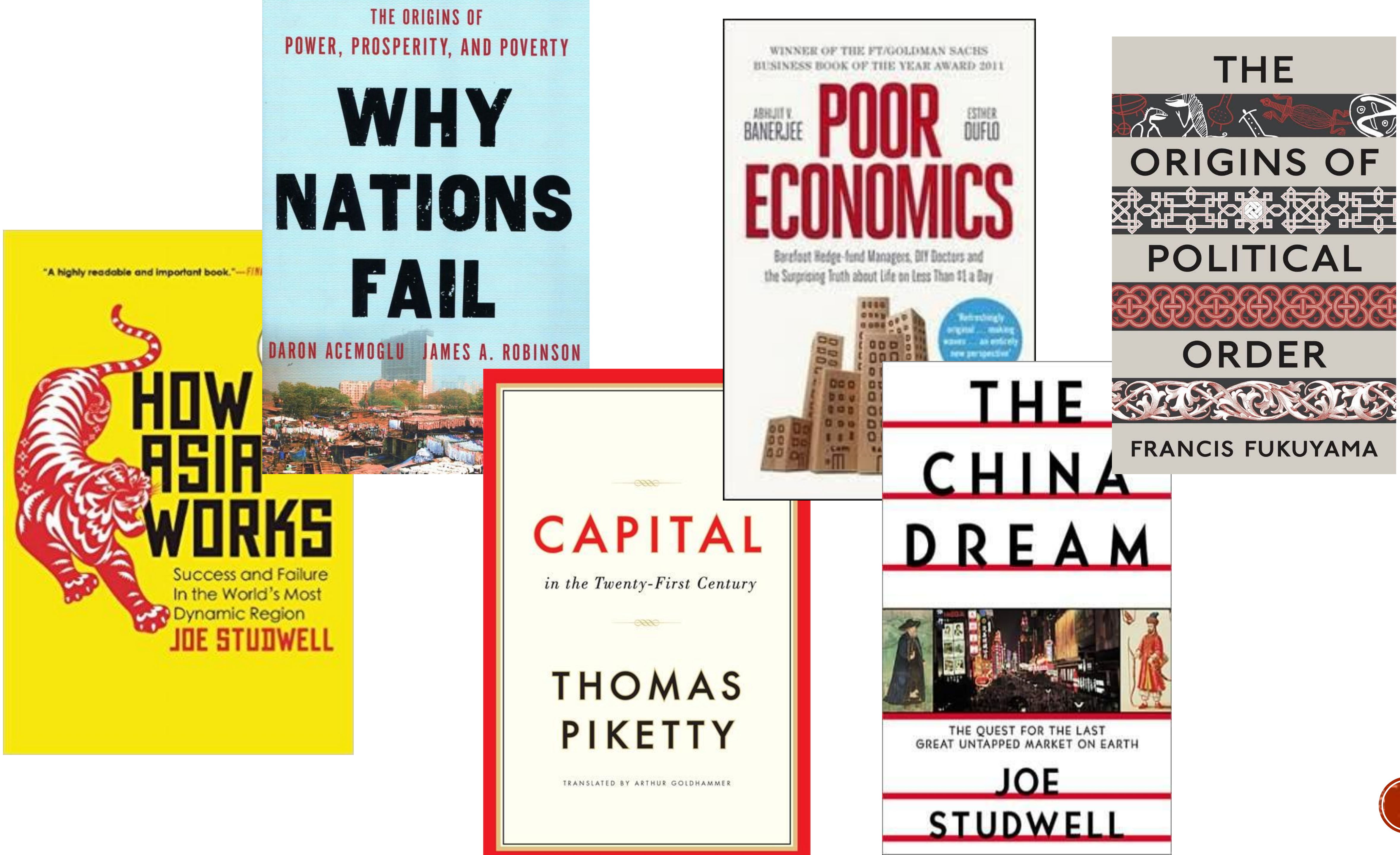
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Success and Failure In the World's Most Dynamic Region
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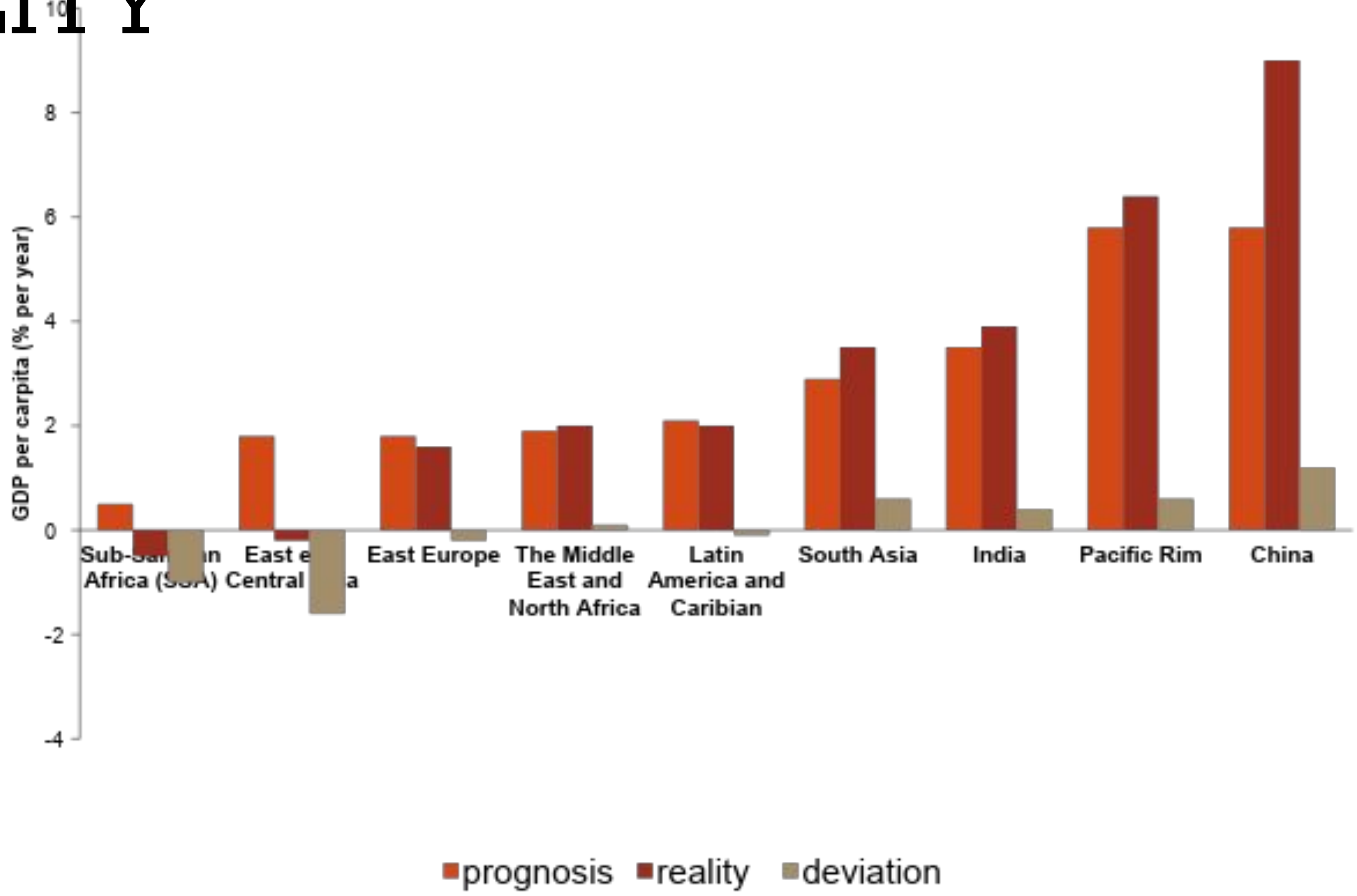
POOR ECONOMICS
ESTHER DUFLO
Barefoot Hedge-fund Managers, DIY Doctors and the Surprising Truth about Life on Less Than $1 a Day
THE CHINA DREAM
THE QUEST FOR THE LAST GREAT UNTAPPED MARKET ON EARTH
JOE STUDWELL
THE ORIGINS OF POLITICAL ORDER
FRANCIS FUKUYAMA

COURSE STRUCTURE

Lesson	Topic
Module 1 *Feb 20*	**Introduction in International Economics:**
Module 2 *Feb 22*	**Meaning of development:** Defining development and undevelopment; How to measure (approaches by IMF, UNDP, WTO); Qualitative and factors of development (GDP vs Inclusive development); Obstacles of development / Problems facing developing countries
Module 3 *Feb 27*	**Theoretical background of international economics:** Linear stages of Growth models; Structural change theories; International dependence theories; Neo-classical, Free-market theories
Module 4 *March 1*	**Modern Factors of Economic Growth and Economic Development:** Economic growth: definition and measurement; economic development of different countries / Interdependence between level of growth and development
Module 5 *March 6*	**Microfinance:** Social impact of Banks; basic mechanism of capital accumulation; public and private investments; human development index (HDI); development indicators
Module 6 *March 13*	**Foreign trade imbalance**: Effectiveness of foreign trade aid; foreign direct investments; capital demand and capital demand specialty; macroeconomic stability
Module 8 *March 15*	**Globalization and Growing Trend to Regionalization:** Globalization – definition, spreading, influence and consequences and opportunities for rich and poor countries
Module 9 *March 22*	**Equality and Economic Growth:** Gender gap, discrimination, pay gap and their consequences for economic growth
Module 10 *March 27*	**Poverty and education:** Poverty and inequality; population growth; access to education
Module 11 *March 29*	**Corruption as a global issue:** Definition, history, best practices of overcoming
Module 12 *April 3*	**Sustainable Development:** Definition and evolution, new economic concept and its applicable variations
Module 13 *April 10*	**Climate and Environment Factors of Sustainable Economic Growth:** Reality or economic mystification; consequences for economic and international relationship
Module 14 *April 12*	**Global Market and Global Competition: Do they encourage or discourage economic growth?**

PROGNOSIS OF COUNTRIES DEVELOPMENT IN 1990^{S} AND REALITY

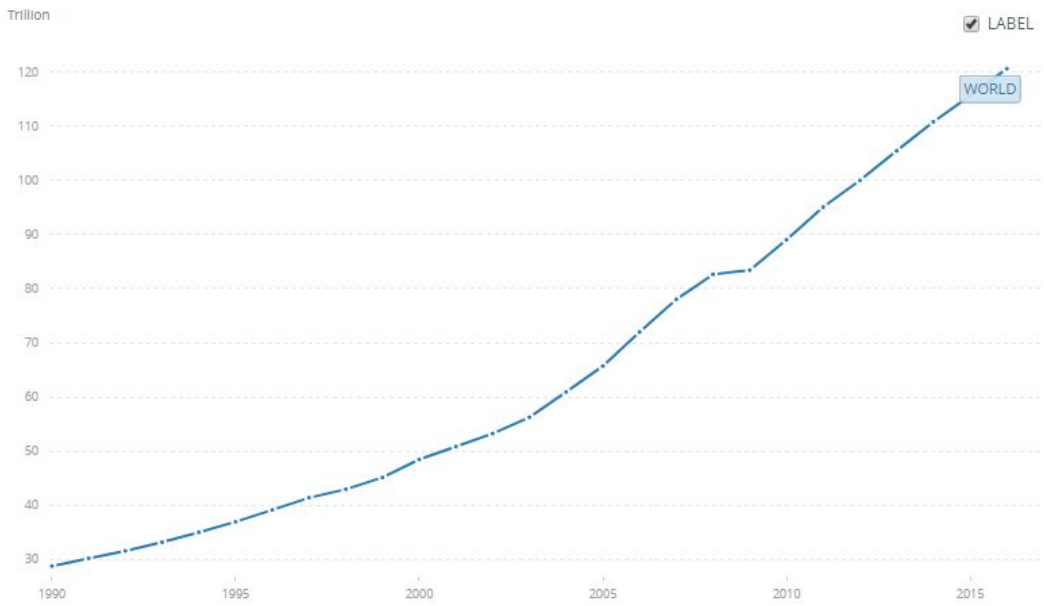


NEW

- The Gross Domestic Product (GDP) of an economy is a measure of total production. More precisely, it is the monetary value of all goods and services produced within a country or region in a specific time period. While the definition of GDP is straightforward, accurately measuring it is a surprisingly difficult undertaking. Moreover, any attempts to make comparisons over time and across borders are complicated by price, quality and currency differences. This article covers the basics of GDP data and highlights many of the pitfalls associated with intertemporal and spatial comparisons.

WORLD DEVELOPMENT IN DYNAMIC

GDP growth (annual %)

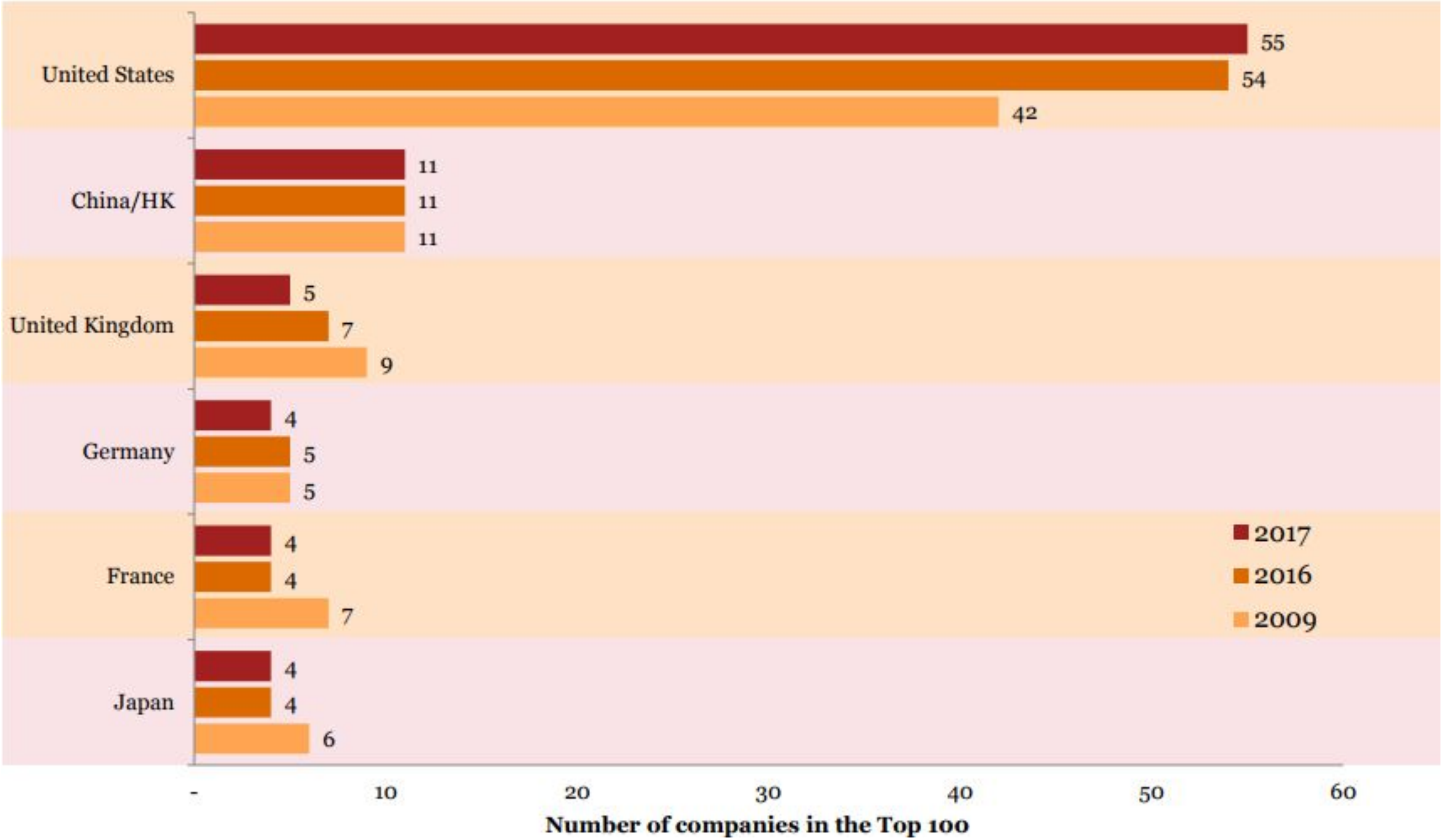


GDP, PPP (current international $)

GDP, GNP, GNI AND GDP PPP

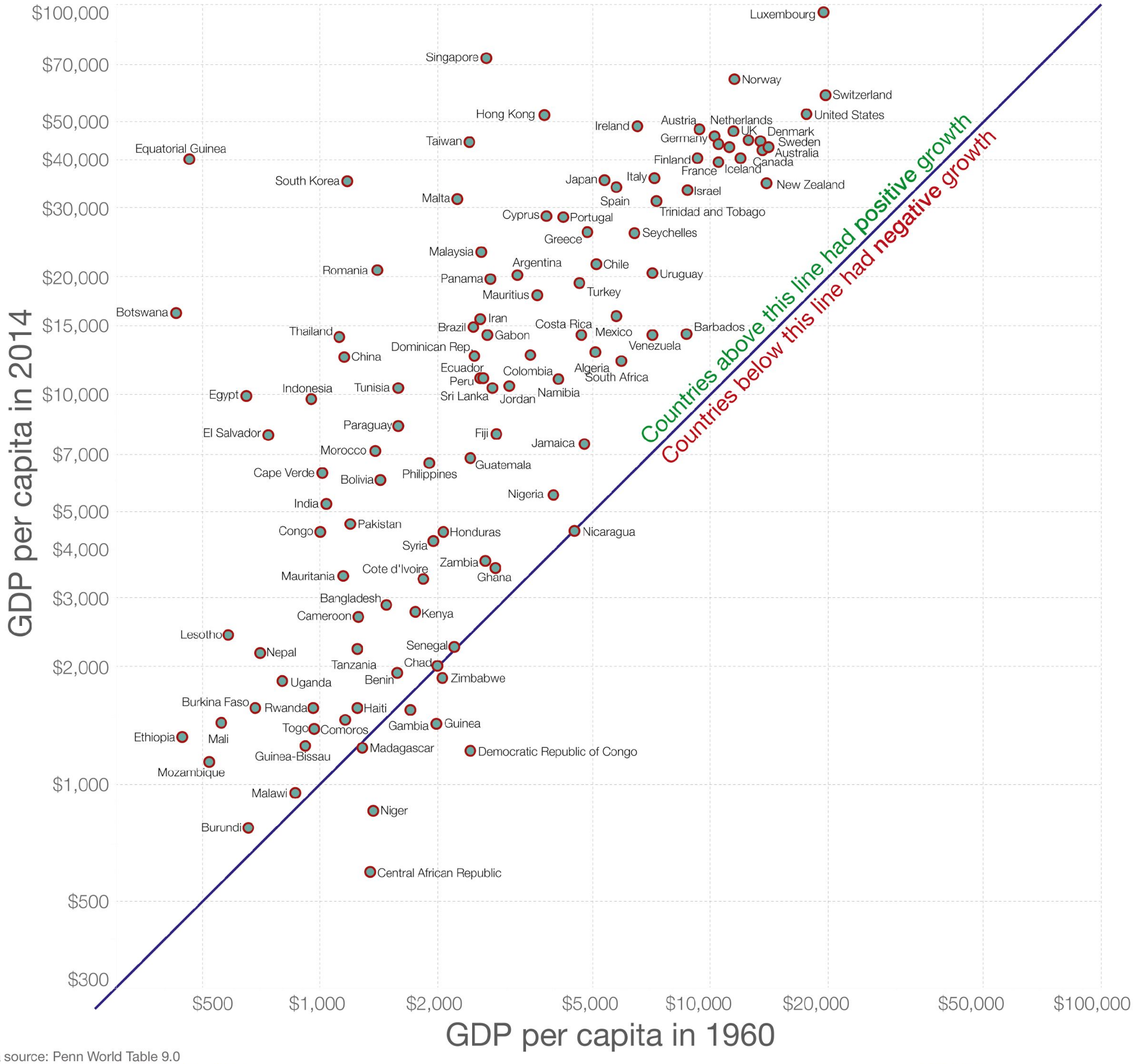
Income Earned by:	GDP	GNI	GNP
Residents in Country	Personal consumption (C) + business investment (I) + government spending (G) + [exports - imports (X)]	GDP +(income from citizens and businesses earned abroad) – (income remitted by foreigners living in the country back to their home countries) __________________ GNP + (income spent by foreigners within the country) – (foreign income not remitted by citizens)	GDP + (income earned on all foreign assets) – (income earned by foreigners in the country)
Foreigners in Country	Includes	Includes If Spent in Country	Excludes All
Residents Out of Country	Excludes	Includes If Remitted Back	Includes All

TOP 100 COMPANIES BY COUNTRY – TRENDS 2009-2017



GDP per capita in 1960 and 2014

GDP per capita is adjusted for price changes over time (inflation) and for price differences between countries (purchasing power parity (PPP) adjustment).

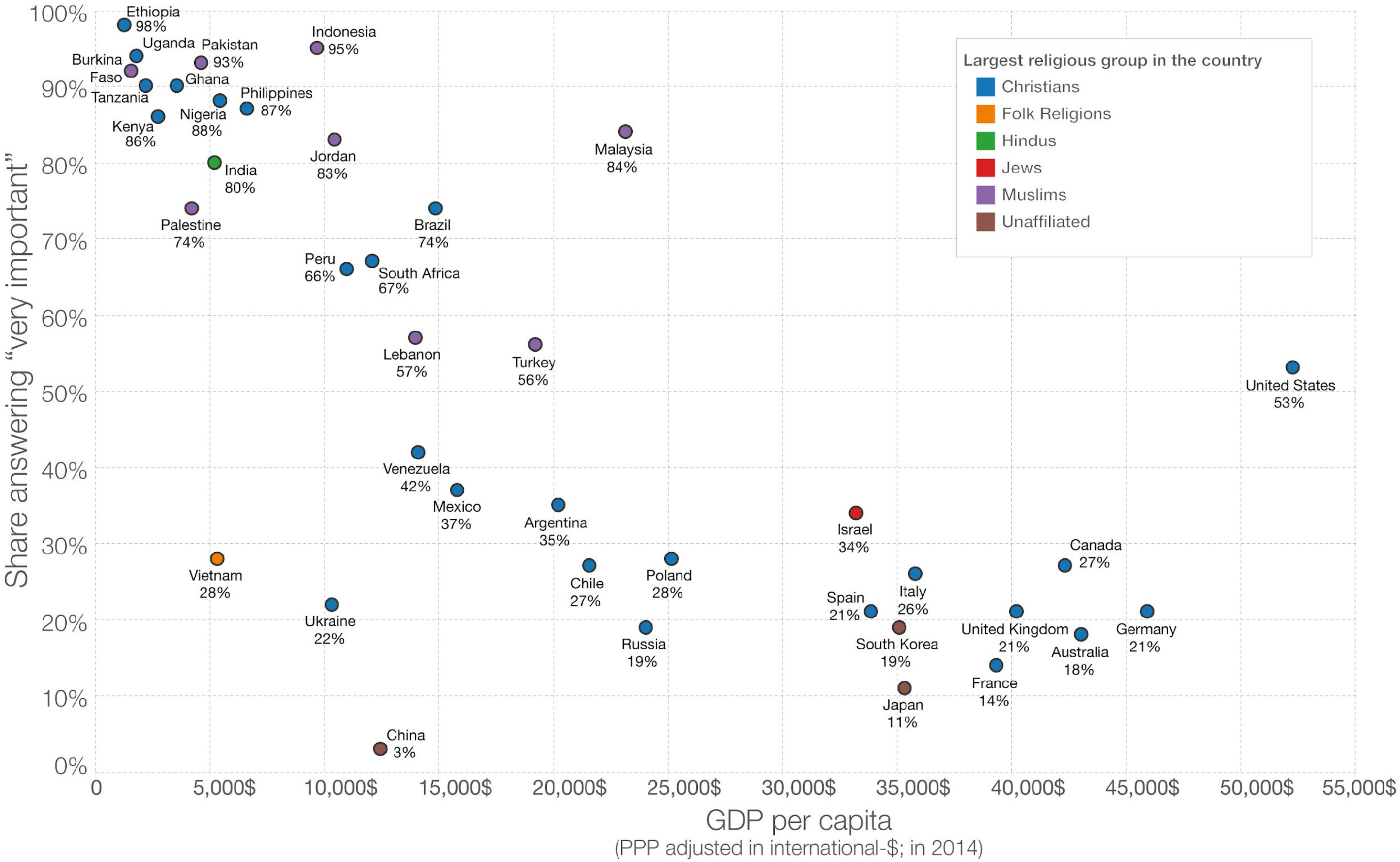


Data source: Penn World Table 9.0

The visualization is available at OurWorldinData.org where you find more visualizations and research on global development.

Importance of Religion vs level of GDP per capita

The question that was asked was "How important is religion in your life?" And the possible answers were "very important", "somewhat important", "not too important" and "not at all important". Shown is the share that answered "very important".
The color of each country represents the largest religion in the county. The percentage value is the share answering very important.



Data source: Penn World Table for GDP per capita; Pew Global Attitudes Survey for importance of religion measure; Pew for majority religion.
The interactive data visualization is available at OurWorldinData.org. There you find the raw data and more visualizations on this topic.

LD

The history of urbanization, 3700 BC – 2000 AD

http://metrocosm.com/history-of-cities/

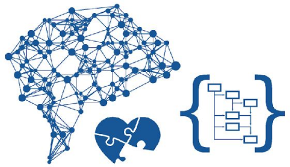
Top 10 skills

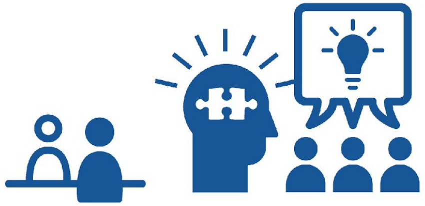
in 2020

1. Complex Problem Solving
2. Critical Thinking
3. Creativity
4. People Management
5. Coordinating with Others
6. Emotional Intelligence
7. Judgment and Decision Making
8. Service Orientation
9. Negotiation
10. Cognitive Flexibility

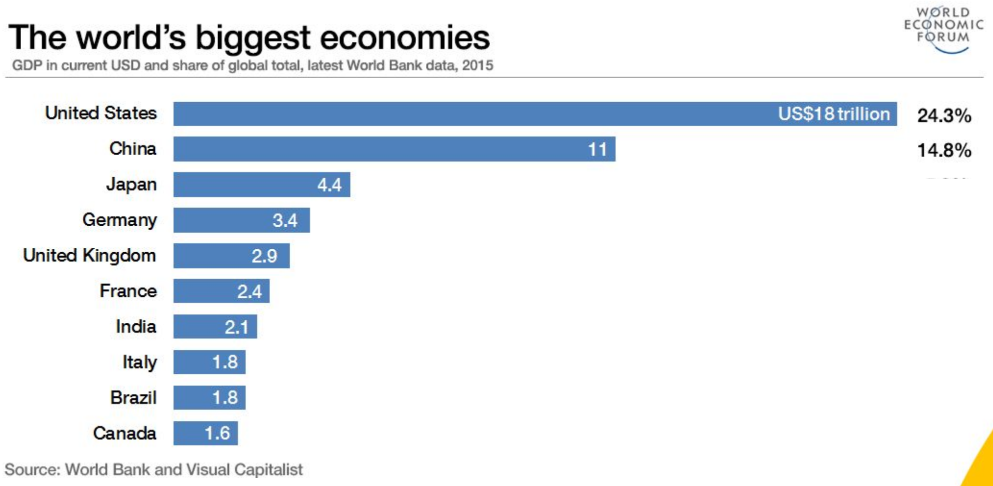
in 2015

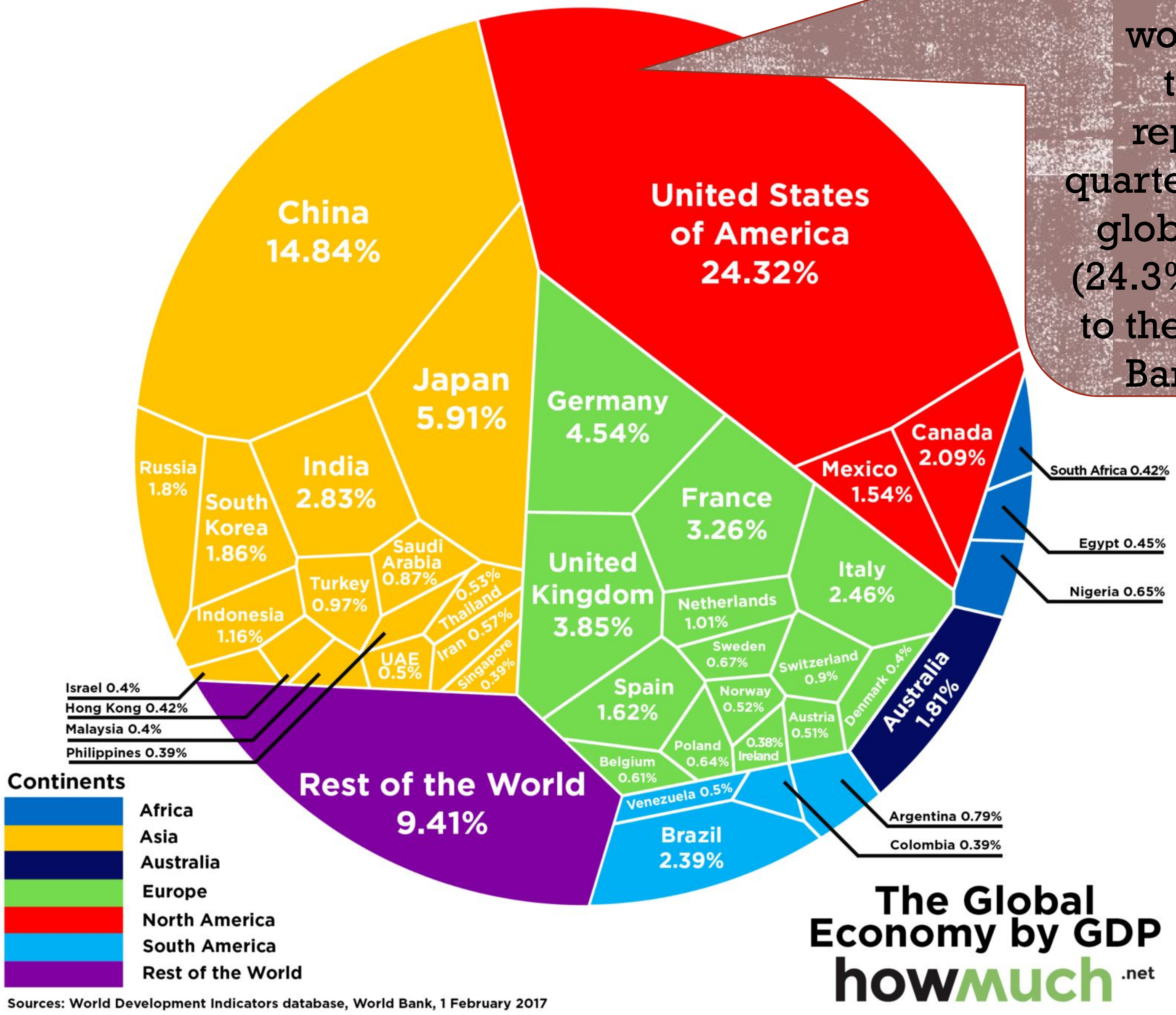
1. Complex Problem Solving
2. Coordinating with Others
3. People Management
4. Critical Thinking
5. Negotiation
6. Quality Control
7. Service Orientation
8. Judgment and Decision Making
9. Active Listening
10. Creativity





Source: Future of Jobs Report, World Economic Forum





The economy of the United States is the largest in the world. At $18 trillion, it represents a quarter share of the global economy (24.3%), according to the latest World Bank figures.

FASTEST-GROWING ECONOMY

- The US may not dominate for much longer, however.
- Although China trails the US by $7 trillion, it's catching up. China's economy grew by **6.7%** in 2016, compared with America's **1.6%**, according to the IMF.
- China has also overtaken India as the fastest-growing large economy. The IMF's World Economic Outlook estimated China's economy grew at 6.7% in 2016, compared with India's 6.6%.
- Brazil's economy has contracted in the last year by 3.5%, the only one in the top 10 to do so.
- The Asian bloc clearly has a larger share than anywhere else, representing just over a third (33.84%) of global GDP. That's compared to North America, which represents just over a quarter, at 27.95%.
- Europe comes third with just over one-fifth of global GDP (21.37%).
- Together, these three blocs generate more than four-fifths (83.16%) of the world's total output.

THE BIGGEST ECONOMIES IN 2050

- A new study by PricewaterhouseCooper says that China will be in first place by 2050, because emerging economies will continue to grow faster than advanced ones.
- India will rank second, the US will be third, and fourth place is expected to go to Indonesia.
- The UK could be down to 10th place by 2050, while France could be out of the top 10 and Italy out of the top 20 as they are overtaken by faster-growing emerging economies such as Mexico, Turkey and Vietnam.
- The report also says that the world economy could more than double in size by 2050, far outstripping population growth, due to technology-driven productivity.

Emerging markets will dominate the world's top 10 economies in 2050 (GDP at PPPs)

	2016	2050	
China	1	1	*China*
US	2	2	*India*
India	3	3	*US*
Japan	4	4	*Indonesia*
Germany	5	5	*Brazil*
Russia	6	6	*Russia*
Brazil	7	7	*Mexico*
Indonesia	8	8	*Japan*
UK	9	9	*Germany*
France	10	10	*UK*

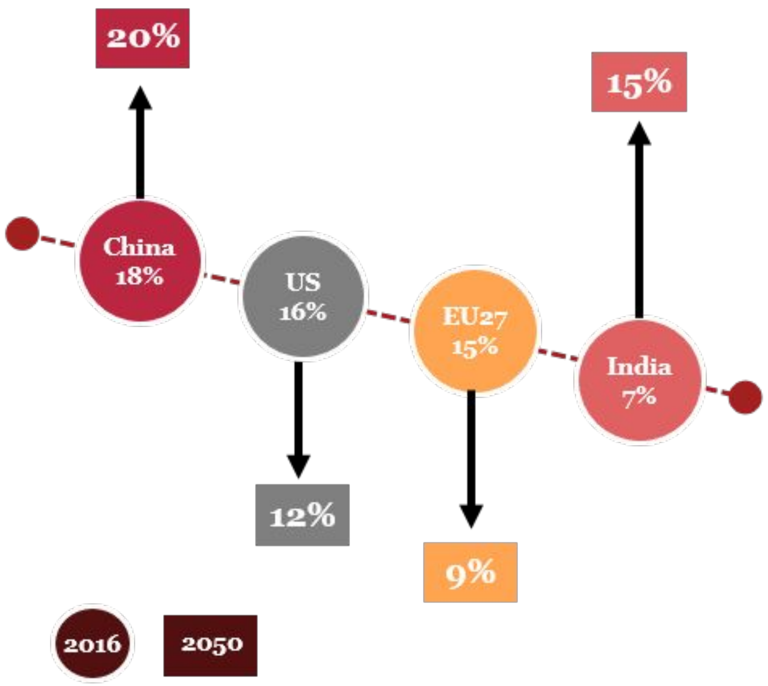
E7 economies G7 economies

Sources: IMF for 2016 estimates, PwC analysis for projections to 2050

THE WORLD IN 2050

The US and Europe will steadily lose ground to China and India

Share of world GDP (PPPs) from 2016 to 2050…



Sources: IMF for 2016 estimates, PwC analysis for projections to 2050

Global economic power will shift to the E7 economies

In…

1995 E7 *were* ***half*** *the size of* G7

By…

2015 E7 *were around the* ***same*** *size as* G7

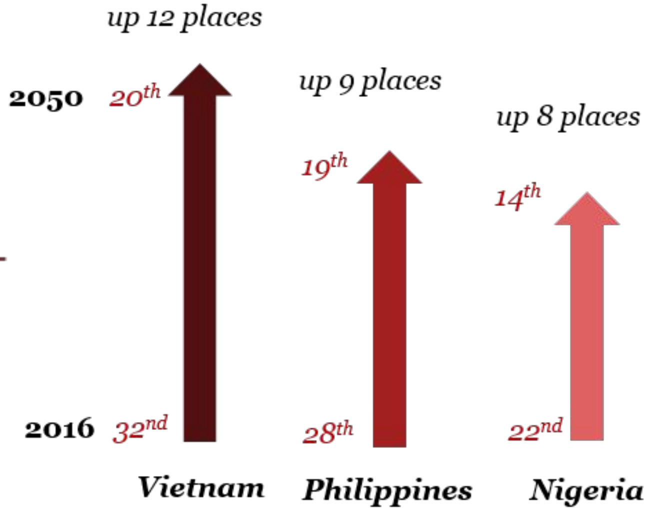
And in just 25 years…

2040 E7 *could be* ***double*** *the size of* G7

G7: US, UK, France, Germany, Japan, Canada and Italy
E7: China, India, Indonesia, Brazil, Russia, Mexico and Turkey

Sources: IMF for historical GDP, PwC analysis for projections to 2050

Vietnam, the Philippines and Nigeria could make the greatest moves up the rankings



Average annual GDP growth rate, 2016-2050

Vietnam	Philippines	Nigeria
5.1%	4.3%	4.2%

Sources: IMF for 2016 estimates, PwC analysis for projections to 2050

RULE 72

- The rule of 72 is a shortcut to estimate the number of years required to double your money at a given annual rate of return.
  - *If Gross Domestic Product (GDP) grows at 4% annually, the economy will be expected to double in 72 ÷ 4 = 18 years.*

GDP grows at 1% - the GDP doubled in 72 years

GDP grows at 7% (the world higher level of growth) – the GDP doubled in 10 years

GDP growth of Ukraine 2,3

China 6,7

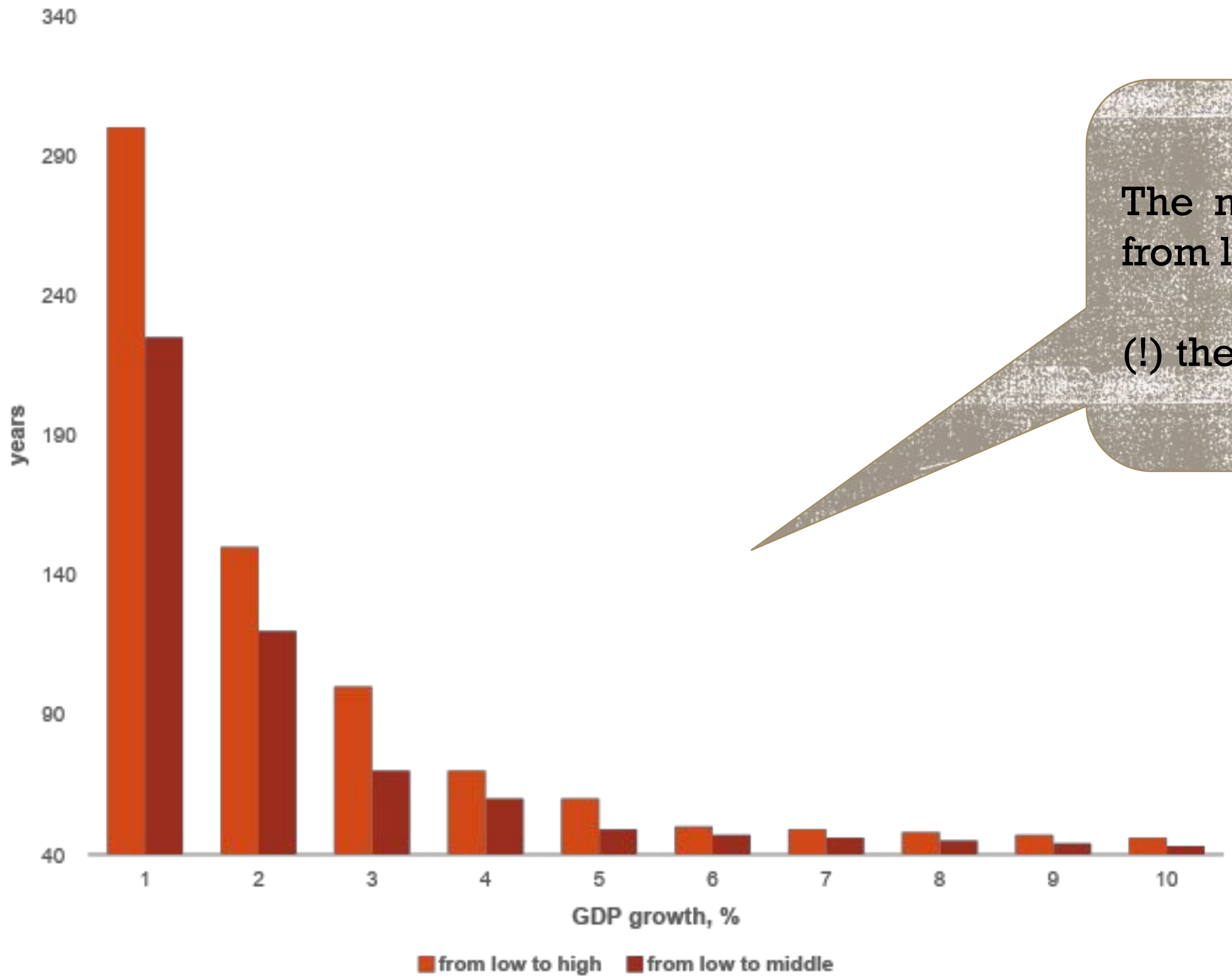
USA 1,5

World 2,24

INCOME

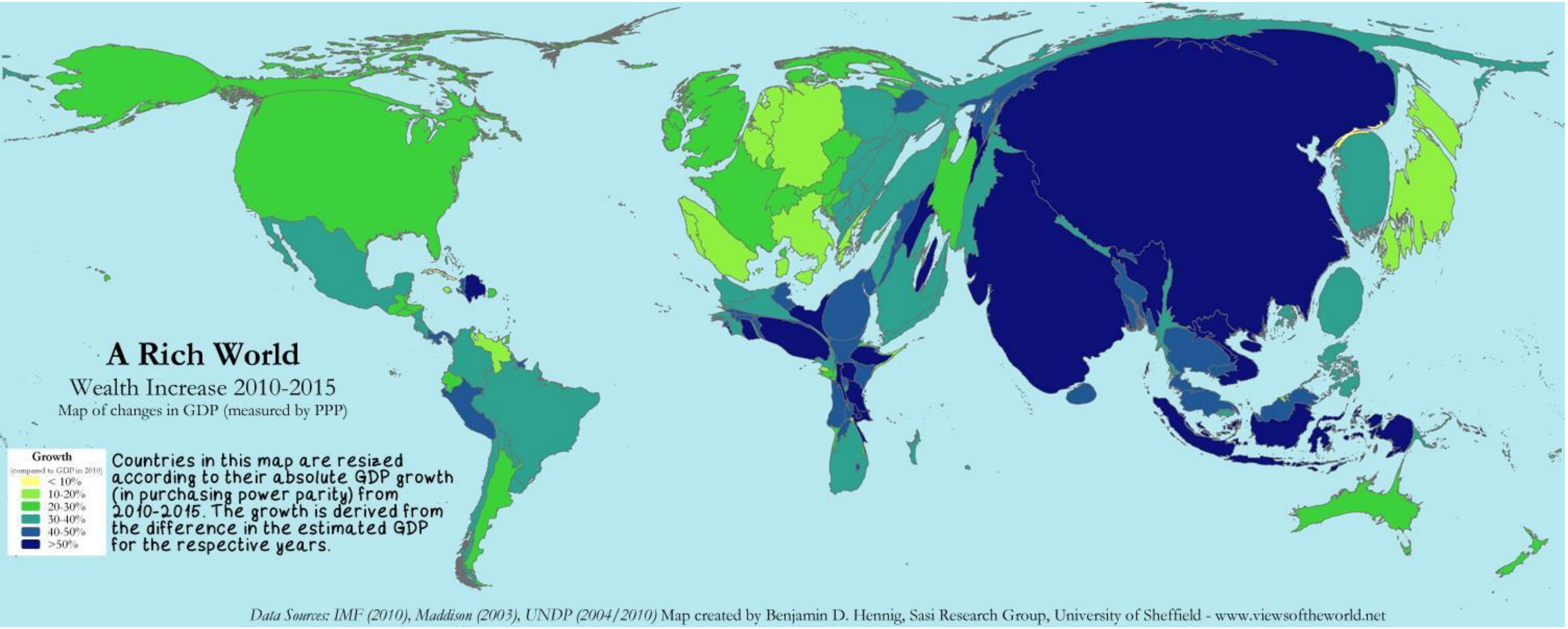
- Incomes per person in poorest countries are $300-500, for developed – above $20,000
- For transition with 7% growth the model will looks like:

The beginning	500
First decade	1,000
2^{nd} decade	2,000
3^{rd} decade	4,000
4^{th} decade	8,000
5^{th} decade	16,000
53-54 years of development	20,000



The most time has spent on growth from low level to middle

(!) the stable growth is important


A Rich World
Wealth Increase 2010-2015
Map of changes in GDP (measured by PPP)
Growth
(compared to GDP in 2010)
< 10%
10-20%
20-30%
30-40%
40-50%
>50%
Countries in this map are resized according to their absolute GDP growth (in purchasing power parity) from 2010-2015. The growth is derived from the difference in the estimated GDP for the respective years.
Data Sources: IMF (2010), Maddison (2003), UNDP (2004/2010) Map created by Benjamin D. Hennig, Sasi Research Group, University of Sheffield - www.viewsoftheworld.net

MEGATRENDS: 5 GLOBAL SHIFTS CHANGING THE WAY WE LIVE AND DO BUSINESS

- Rapid urbanization
- Climate change & resource scarcity
- Shift in global economic power
- Demographic and social change
- Technological breakthroughs

WORLD ECONOMICS: MEANING OF DEVELOPMENT

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DEVELOPMENT

- What is the difference between growth and development?
  - **Economic growth** means an increase in real national income / national output.
  - **Economic development** means an improvement in the quality of life and living standards, e.g. measures of literacy, life-expectancy and health care.
  - Ceteris paribus, we would expect economic growth to enable more economic development. Higher real GDP enables more to be spent on health care and education.
  - However, the link is not guaranteed. The proceeds of economic growth could be wasted or retained by a small wealthy elite.

DEVELOPED AND DEVELOPING COUNTRIES

- The primary factor used to distinguish developed countries from developing countries is gross domestic product (GDP) per capita, a figure calculated by dividing a country's GDP by its population.

- One unofficial threshold for a country with a developed economy is a GDP per capita of $12,000. Some economists prefer to see a per capita GDP of at least $25,000 to be comfortable declaring a country as developed, however. Many highly developed countries, including the United States, have high per capita GDPs of $40,000 or above.

DIFFERENCES BETWEEN DEVELOPED AND DEVELOPING COUNTRIES

Exceeding even the $12,000 GDP does not automatically qualify a country as being developed. Developed countries share several other characteristics:

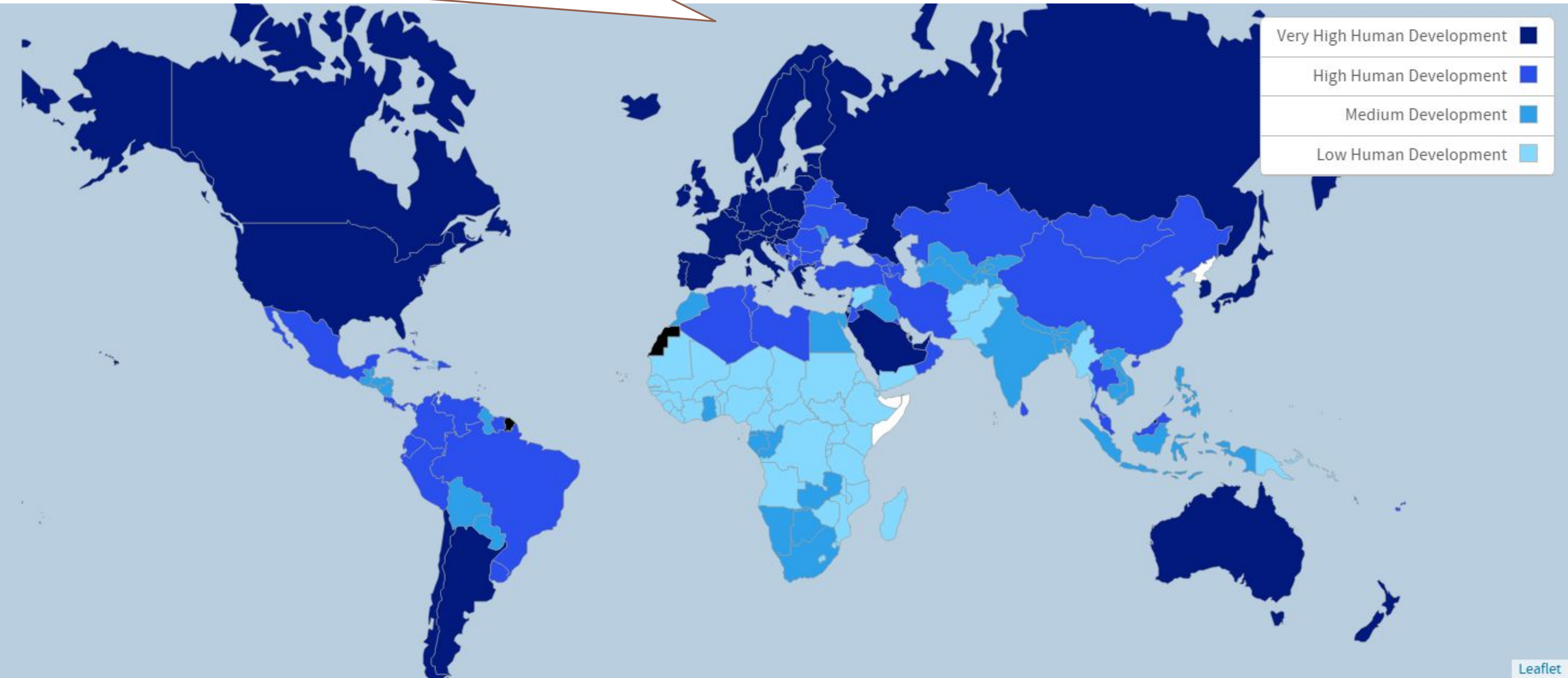
- They are highly industrialized.
- Their birth and death rates are stable. They do not have excessively high birth rates because, thanks to quality medical care and high living standards, infant mortality rates are low. Families do not feel the need to have high numbers of children with the expectation that some will not survive. No developed country has an infant mortality rate higher than 10 per 1,000 live births. In terms of life expectancy, all developed countries boast numbers greater than 70 years; many average 80.
- They have more women working, particularly in high-ranking executive positions. These career-oriented women frequently choose to have smaller families or eschew having children altogether.
- They use a disproportionate amount of the world's resources, such as oil. In developed countries, more people drive cars, fly on airplanes, and power their homes with electricity and gas. Inhabitants of developing countries often do not have access to technologies that require the use of these resources.
- They have higher levels of debt. Nations with developing economies cannot obtain the kind of seemingly bottomless financing that more developed nations can.

HOW TO MEASURE DEVELOPMENT

Institutions measure a country's level of development in many different ways. For instance, the United Nations has few conventions for distinguishing between "developed" and "developing" countries, while the World Bank makes specific distinctions using gross national income (GNI) per capita, although other analytical tools may be used in the process.

- The **International Monetary Fund's** (IMF) definition is often considered to be the most comprehensive measure since it takes into account per capita income, export diversification, and the degree of integration into the global financial system. In 2011, the organization published a research report on the topic of classification titled "Classification of Countries Based on Their Level of Development" that outlines its methodologies for classifying a country's level of development.
- The **World Bank** has a much more concrete methodology as it considers countries with per capita income of less than US$12,275 as "developing" countries. But the organization also divides these developing countries into numerous income classes, ranging from low-income to upper-middle-income countries, meaning there are other gray areas for international investors to consider.
- There are no **WTO** definitions of "developed" and "developing" countries. Members announce for themselves whether they are "developed" or "developing" countries.

Another measuring device: the **HUMAN DEVELOPMENT INDEX** (HDI) developed by the United Nations as a metric to assess the social and economic development levels of countries. It quantifies life expectancy, educational attainment and income into a standardized number between 0 and 1; the closer to 1, the more developed the country. No minimum requirement exists for developed status, but most developed countries have HDIs of 0.8 or higher.



TYPICALLY RECOGNIZED DEVELOPING COUNTRIES

- Different organizations use different measures to determine how companies are classified, but a few common denominators appear in the mix. For instance, the so-called BRICS are generally considered developing countries and comprise Brazil, Russia, India, China, and South Africa, but examples of common developing countries go far beyond these popular emerging markets.
- Some other countries that appear on include the following:

- Argentina.
- Chile.
- Malaysia.
- Mexico.
- Pakistan.

WHO NEEDS CLASSIFICATIONS OF COUNTRIES TO DEVELOP AND DEVELOPING

International investors often classify countries around the world based on their level of economic development. These classifications are based on a number of economic and social criteria, ranging from per capita income to life expectancy to literacy rates.

These classifications are

- Developed countries,
- Developing countries,
- Less developed countries and
- Emerging markets

WHAT ARE FRONTIER & EMERGING MARKETS?

Frontier and emerging markets

- spanning from **Africa** to **Latin America** and beyond
- represent some of the **fastest growing economies** in the world.

- Emerging markets is a term that was coined in the 1980s to represent countries transitioning from developing to developed status. While the term is commonly used among investors, there is *no universally accepted definition of emerging markets*.
- When emerging market economies began to mature, the term frontier markets was coined to represent investable countries with lower market capitalizations and liquidity. These countries are widely considered to be the up-and-coming emerging markets, but are a bit more hazardous to investors in terms of political risk, market maturity, and transparency.

- The emerging markets in 2017 were:

- Brazil,
- Chile,
- China,
- Colombia,
- Czech Republic,
- Egypt,
- Greece,
- Hungary,

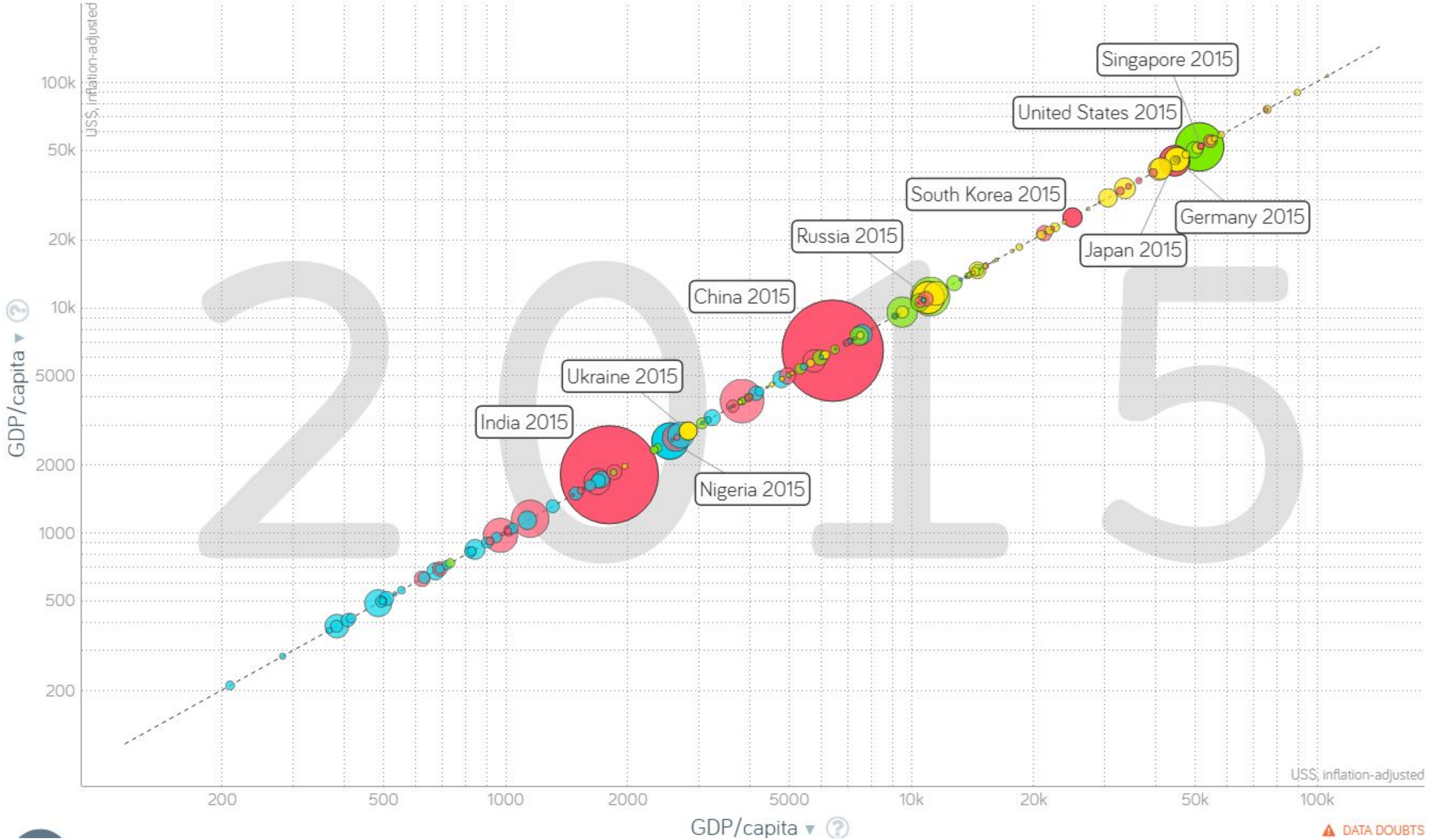
- India,
- Indonesia,

FRONTIER MARKETS

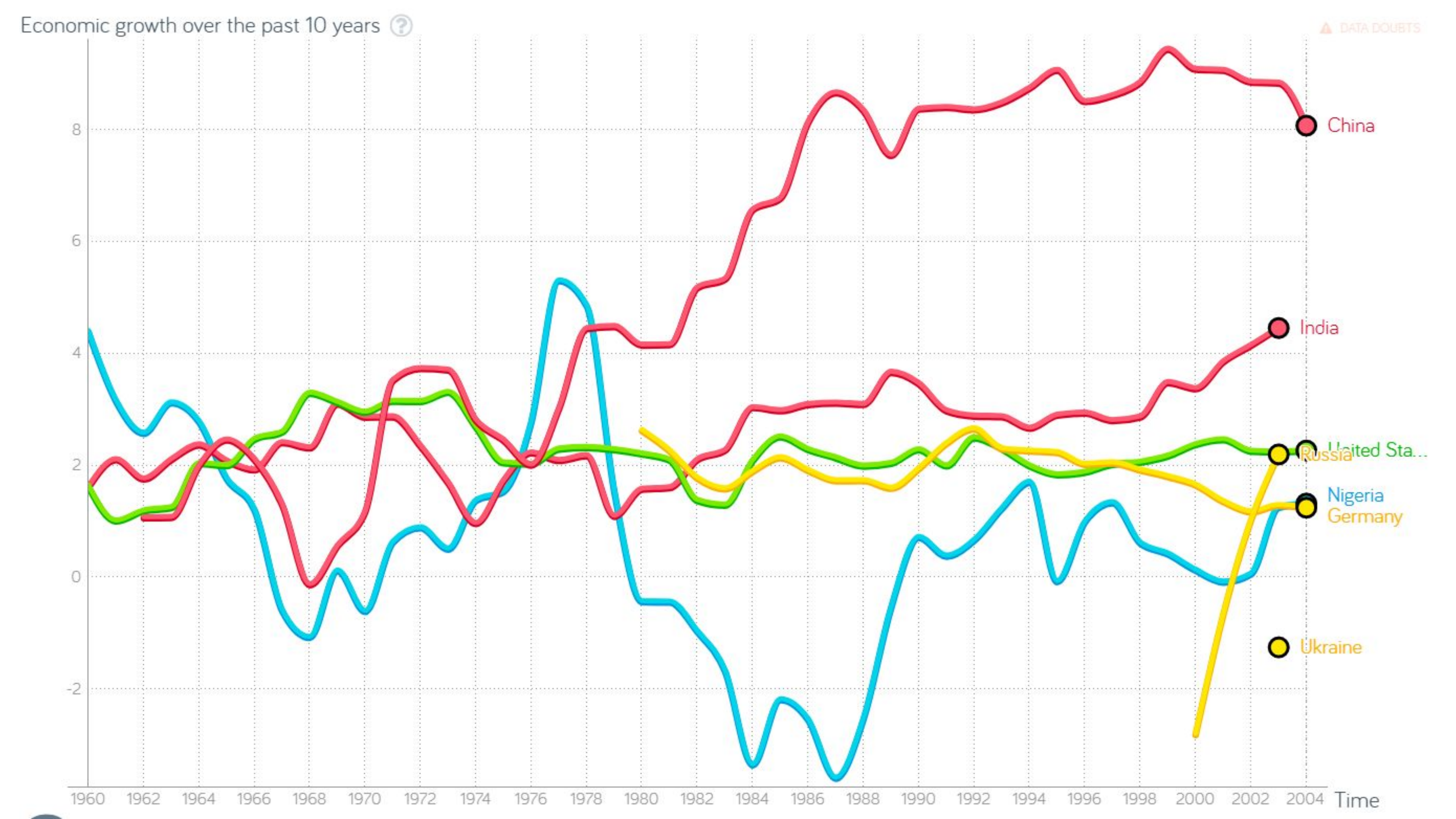
- Frontier and emerging markets offer investors higher potential returns, but they also involve greater risk than developed countries like the United States. This attributes make them ideal for investors with a medium to long-term time horizon.
- There is no single definition of a frontier market or emerging market, but instead, there are several different indices. Many of these indices have ETFs that offer investors a quick way to diversify in these high growth markets.
- Investors looking for either more specific exposure or broader exposure have several alternatives to all-world funds.

COUNTRY CLASSIFICATION SYSTEMS IN SELECTED INTERNATIONAL ORGANIZATIONS

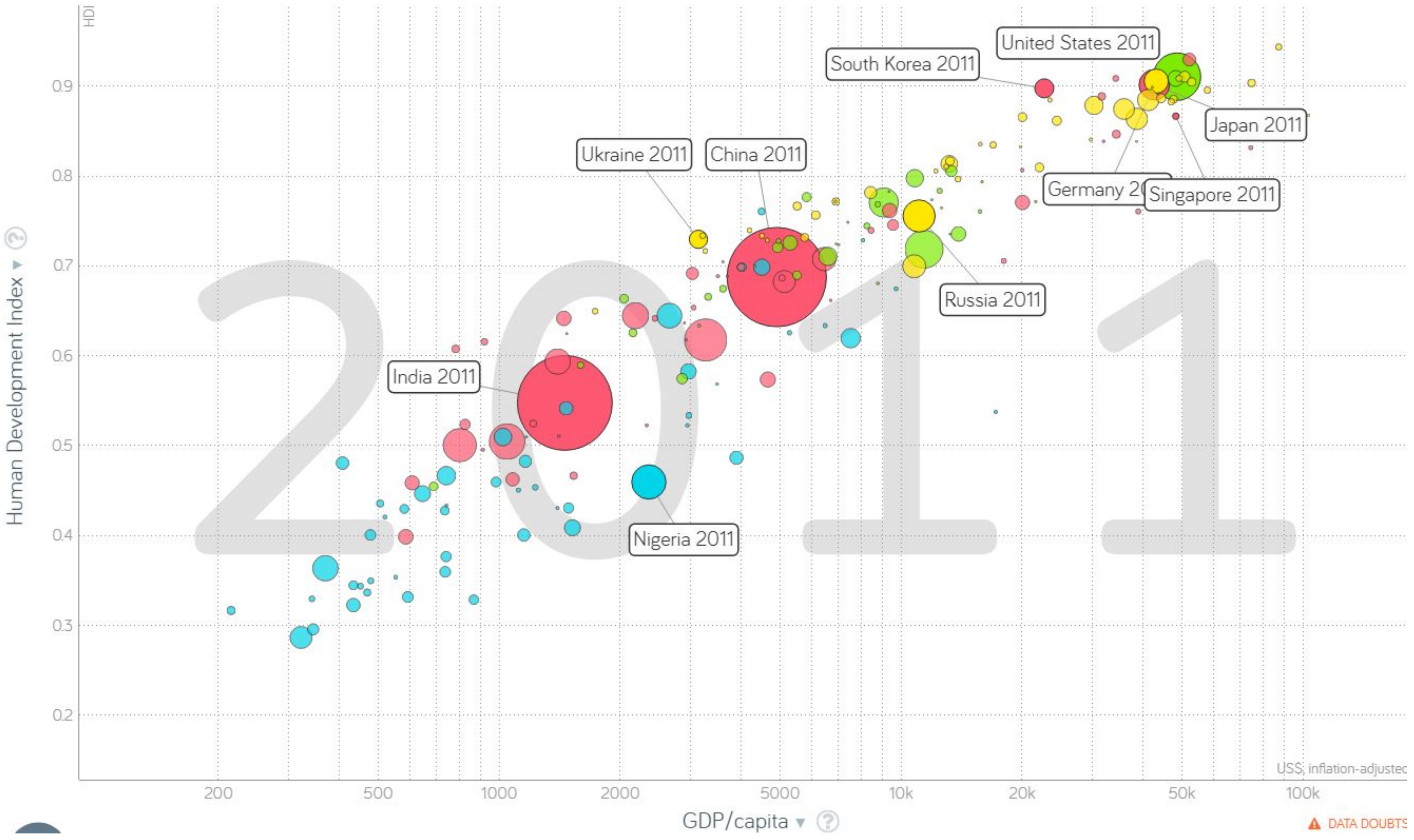
	IMF	UNDP	World Bank
Name of 'developed countries'	Advanced countries	Developed countries	High-income countries
Name of 'developing countries'	Emerging and developing countries	Developing countries	Low- and middle income countries
Development threshold	Not explicit	75 percentile in the HDI distribution	US$6,000 GNI per capita in 1987-prices
Share of countries 'developed' in 1990	13 percent	25 percent	16 percent
Share of countries 'developed' in 2010	17 percent	25 percent	26 percent
Subcategories of 'developing countries'	(1) Low-income developing countries and (2) Emerging and other developing countries	(1) Low human development countries, (2) Medium human development countries, and (3) High human development countries	(1) Low-income countries and (2) Middle-income countries



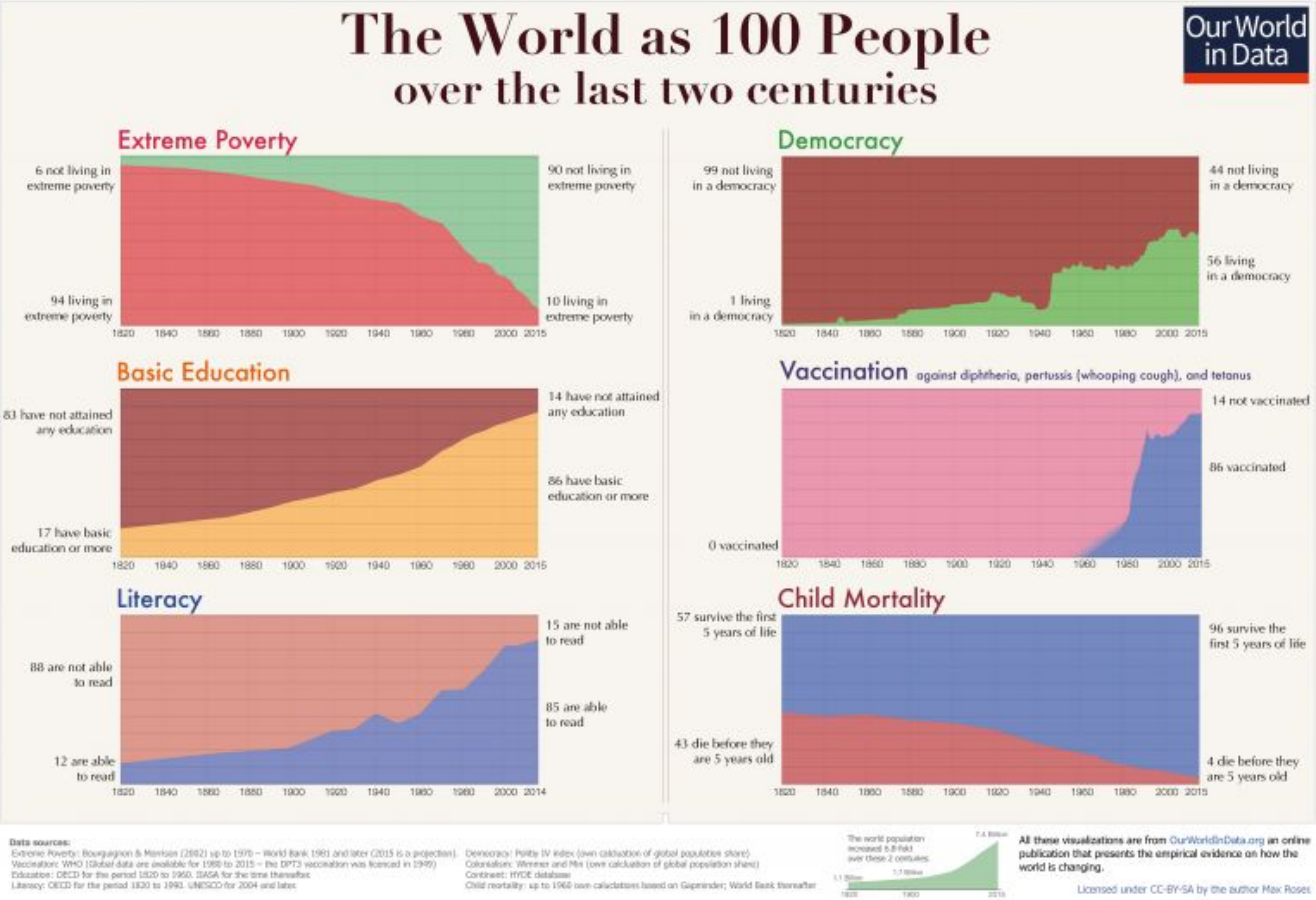
Singapore 2015
United States 2015
South Korea 2015
Germany 2015
Japan 2015
Russia 2015
China 2015
Ukraine 2015
India 2015
Nigeria 2015
2015
100k
50k
20k
10k
5000
2000
1000
500
200
GDP/capita
US$, inflation-adjusted
200
500
1000
2000
5000
10k
20k
50k
100k
GDP/capita
US$, inflation-adjusted
DATA DOUBTS



Economic growth over the past 10 years
DATA DOUBTS
8
6
4
2
0
-2
1960
1962
1964
1966
1968
1970
1972
1974
1976
1978
1980
1982
1984
1986
1988
1990
1992
1994
1996
1998
2000
2002
2004
Time
China
India
United Sta...
Russia
Nigeria
Germany
Ukraine



HDI
Human Development Index
GDP/capita
United States 2011
South Korea 2011
Japan 2011
Ukraine 2011
China 2011
Germany 2
Singapore 2011
Russia 2011
India 2011
Nigeria 2011
2011
0.9
0.8
0.7
0.6
0.5
0.4
0.3
0.2
200
500
1000
2000
5000
10k
20k
50k
100k
US$, inflation-adjusted
DATA DOUBTS


The World as 100 People
over the last two centuries
Our World in Data
Extreme Poverty
6 not living in extreme poverty
94 living in extreme poverty
90 not living in extreme poverty
10 living in extreme poverty
Democracy
99 not living in a democracy
1 living in a democracy
44 not living in a democracy
56 living in a democracy
Basic Education
83 have not attained any education
17 have basic education or more
14 have not attained any education
86 have basic education or more
Vaccination against diphtheria, pertussis (whooping cough), and tetanus
0 vaccinated
14 not vaccinated
86 vaccinated
Literacy
88 are not able to read
12 are able to read
15 are not able to read
85 are able to read
Child Mortality
57 survive the first 5 years of life
43 die before they are 5 years old
96 survive the first 5 years of life
4 die before they are 5 years old
1820 1840 1860 1880 1900 1920 1940 1960 1980 2000 2015
Data sources:
Extreme Poverty: Bourguignon & Morrison (2002) up to 1970 – World Bank 1981 and later (2015 is a projection).
Vaccination: WHO (Global data are available for 1980 to 2015 – the DPT3 vaccination was licenced in 1949)
Education: OECD for the period 1820 to 1960. IIASA for the time thereafter.
Literacy: OECD for the period 1820 to 1990. UNESCO for 2004 and later.
Democracy: Polity IV index (own calculation of global population share)
Colonialism: Wimmer and Min (own calculation of global population share)
Continent: HYDE database
Child mortality: up to 1960 own calculations based on Gapminder; World Bank thereafter
The world population increased 6.8-fold over these 2 centuries.
All these visualizations are from OurWorldInData.org an online publication that presents the empirical evidence on how the world is changing.
Licensed under CC-BY-SA by the author Max Roser.

TRENDS OF MODERN ECONOMICS

Arcelor Mittal (Krivirizhstal)

The most expensive Ukrainian privatization - $ 5 billions

At the time of privatization – 52,000 workers

WhatsApp

Company founded by Jan Koum (borne in Kyiv)

Sold for $19 billions

At the time f sale – 57 workers

TRENDS OF MODERN ECONOMICS

Wheat harvest in Ukraine
20 million tons
Market price = 220 $ / ton
Total = $ 4.4 billion

Avatar movie

World movie rental - $ 2.8 billion

WORLD ECONOMICS: THEORETICAL BACKGROUND OF INTERNATIONAL ECONOMICS

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LINEAR-STAGES-OF-GROWTH MODELS

- Development theory is a conglomeration of theories about how desirable change in society is best achieved.
- The Linear Stages of Growth model is an economic model which is heavily inspired by the Marshall Plan of the US which was used to rehabilitate Europe's economy after the Post-World War II Crisis.
- The linear stages of growth models are the oldest and most traditional of all development plans. It was an attempt by economists to come up with a suitable concept as to how underdeveloped countries of Asia, Africa and Latin America can transform their agrarian economy into an industrialized one.
- The most popular of the linear stage models are Rostow's Stages of Growth Model and the Harrod-Domar Growth Model.

ROSTOW - FIVE STAGES OF ECONOMIC GROWTH MODEL

1. **Traditional society**. This is an agricultural economy of mainly subsistence farming, little of which is traded. The size of the capital stock is limited and of low quality resulting in very low labour productivity and little surplus output left to sell in domestic and overseas markets
2. **Pre-conditions for take-off**. Agriculture becomes more mechanised and more output is traded. Savings and investment grow although they are still a small percentage of national income (GDP). Some external funding is required - for example in the form of overseas aid or perhaps remittance incomes from migrant workers living overseas
3. **Take-off**. Manufacturing industry assumes greater importance, although the number of industries remains small. Political and social institutions start to develop - external finance may still be required. Savings and investment grow, perhaps to 15% of GDP. Agriculture assumes lesser importance in relative terms although the majority of people may remain employed in the farming sector. There is often a dual economy apparent with rising productivity and wealth in manufacturing and other industries contrasted with stubbornly low productivity and real incomes in rural agriculture.
4. **Drive to maturity**. Industry becomes more diverse. Growth should spread to different parts of the country as the state of technology improves - the economy moves from being dependent on factor inputs for growth towards making better use of innovation to bring about increases in real per capita incomes
5. **Age of mass consumption**. Output levels grow, enabling increased consumer expenditure. There is a shift towards tertiary sector activity and the growth is sustained by the expansion of a middle class of consumers.

HARROD-DOMAR MODEL

- This model was developed independently by Roy F. Harrod in 1939 and Evsey Domar in 1946.
- Model is an early post-Keynesian model of economic growth. It is used in development economics to explain an economy's growth rate in terms of the level of saving and productivity of capital.
- The Harrod-Domar Model is based on a linear function and can also be referred to as the AK model where A is a constant and K is capital stock. This model shows how sufficient investment through savings can accelerate growth. Investments generate income and supplements productivity of the economy by increasing the capital stock.
- The Harrod-Domar model is based on the following assumptions:
  - ✓ *Laissez-faire; where there is no government intervention*
  - ✓ *A closed economy; no participation in foreign trade*
  - ✓ *Capital goods do not depreciate as they possess a boundless timeline*
  - ✓ *Constant marginal propensity to save*
  - ✓ *Interest rate remains unchanged, etc.*

HARROD-DOMAR MODEL

The Harrod-Domar model makes use of a **Capital-output Ratio (COR)**. If the COR is low a country can produce more with little capital but if it is high, more capital is required for production and value of output is less. This can be denoted in a simple formula of K/Y=COR; where K is the Capital stock and Y is Output because there is a direct proportional relationship between both variables.

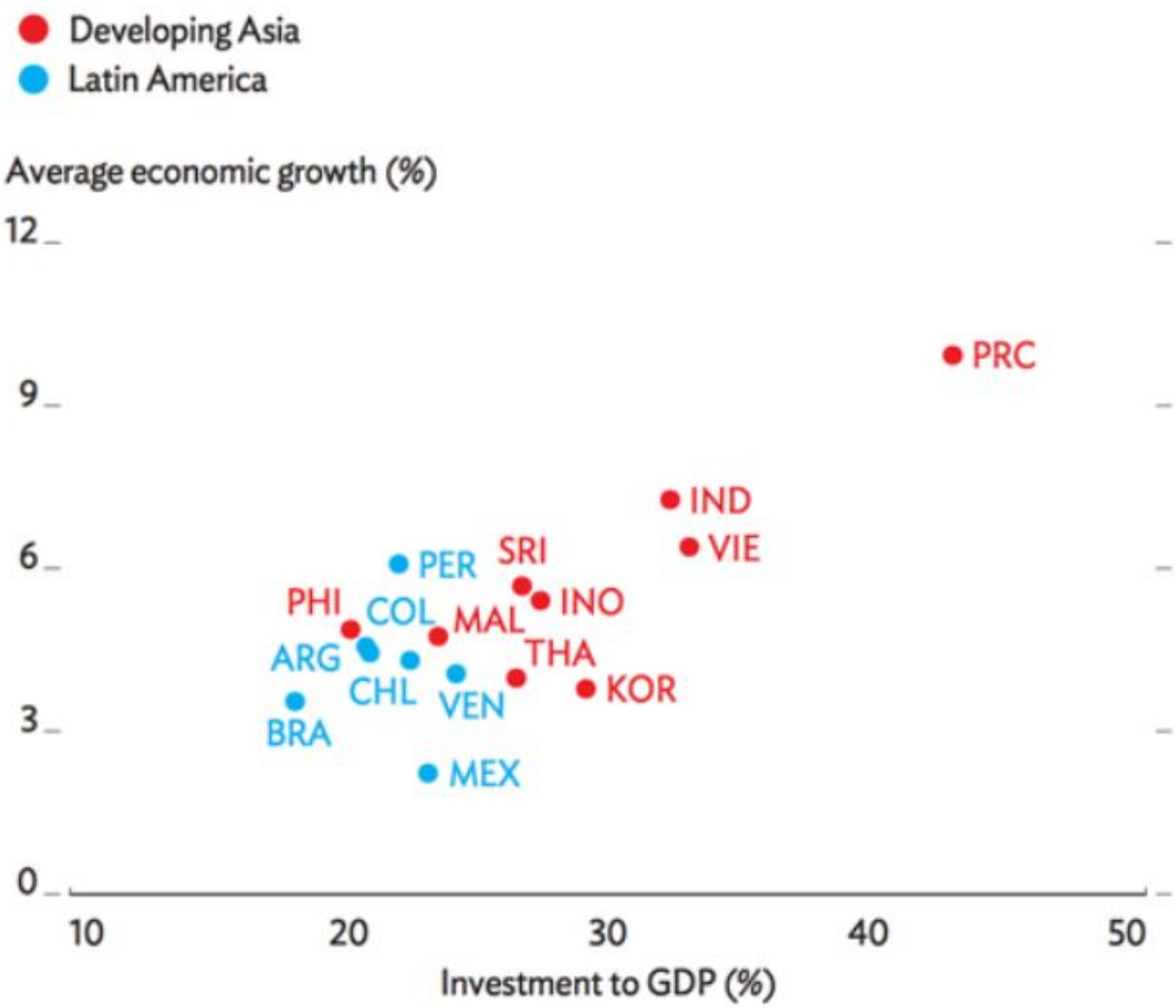
Rate of growth of GDP = Savings Ratio / Capital Output Ratio

Numerical examples:

- If the savings rate is 10% and the capital output ratio is 2, then a country would grow at 5% per year.
- If the savings rate is 20% and the capital output ratio is 1.5, then a country would grow at 13.3% per year.
- If the savings rate is 8% and the capital output ratio is 4, then the country would grow at 2% per year.

Based on the model therefore the rate of growth in an economy can be increased in one of two ways:

- Increased level of savings in the economy (i.e. gross national savings as a % of GDP)
- Reducing the capital output ratio (i.e. increasing the quality / productivity of capital inputs)



ARG = Argentina, BRA = Brazil, CHL = Chile, COL = Colombia, IND = India, INO = Indonesia, KOR = Republic of Korea, MAL = Malaysia, MEX = Mexico, PER = Peru, PHI = Philippines, PRC = People's Republic of China, SRI = Sri Lanka, THA = Thailand, VEN = Venezuela, VIE = Viet Nam.

Source: International Monetary Fund 2014.

SOME OF THE KEY LIMITATIONS / PROBLEMS OF THE HARROD-DOMAR GROWTH MODEL

- Increasing the savings ratio in lower-income countries is not easy. Many developing countries have low marginal propensities to save. Extra income gained is often spent on increased consumption rather than saved. Many countries suffer from a persistent domestic savings gap.
- Many developing countries lack a sound financial system. Increased saving by households does not necessarily mean there will be greater funds available for firms to borrow to invest.
- Efficiency gains that reduce the capital/output ratio are difficult to achieve in developing countries due to weaknesses in human capital, causing capital to be used inefficiently
- Research and development (R&D) needed to improve the capital/output ratio is often under-funded - this is a cause of market failure
- Borrowing from overseas to fill the savings gap causes external debt repayment problems later.
- The accumulation of capital will increase if the economy starts growing dynamically – a rise in capital spending is not necessarily a pre-condition for economic growth and development – as a country gets richer, incomes rise, so too does saving, and the higher income fuels rising demand which itself prompts a rise in capital investment spending.

EVALUATION OF 5 STAGES OF ECONOMIC GROWTH MODEL

- There is overlap with the **Harrod-Domar** model i.e. stages 2 and 3 require increased saving and investment; Stage 4 requires improvements in technology, which reduces the capital-output ratio.
- Stages 2 and 3 call for increased savings and investment but many households may not have the funds to save; the banking channel between savers and firms may be inadequate; the productivity of individual investment projects may depend upon complementary investment in infrastructure.
- Some Sub Saharan African countries have received significant external finance but have been slow to generate growth - many have remained stuck in Stages 1 or 2.
- When the external finance has come in the shape of loans from developed countries, interest charges have been incurred which have acted as a drag on economic growth.
- **Simon Kuznets** threw doubts upon Rostow's theory. He argued that many countries which have now reached developed status did so without seeing a significant increase in their savings rate.
- The theory does not account for exceptions, e.g. falling output in the USSR under a communist regime; the corrupt and failing government in Zimbabwe has reversed development advances; increased globalisation means that a country's growth rate does not lie solely in its own hands and international competition and protectionism may prevent an economy from moving through the latter stages.

LEWIS 2-SECTORS MODEL

- Arthur Lewis put forward a development model of a **DUALISTIC** economy, consisting of rural agricultural and urban manufacturing sectors
- Initially, the majority of labour is employed upon the land, which is a fixed resource. Labour is a variable resource and, as more labour is put to work on the land, diminishing marginal returns eventually set in: there may be insufficient tasks for the marginal worker to undertake, resulting in reduced marginal product (output produced by an additional worker) and underemployment.
- Urban workers, engaged in manufacturing, tend to produce a higher value of output than their agricultural counterparts. The resultant higher urban wages (Lewis stated that a 30% premium was required) might therefore tempt surplus agricultural workers to migrate to cities and engage in manufacturing activity. High urban profits would encourage firms to expand and hence result in further rural-urban migration.

THE LEWIS MODEL IS A MODEL OF STRUCTURAL CHANGE SINCE IT OUTLINES THE DEVELOPMENT FROM A TRADITIONAL ECONOMY TO AN INDUSTRIALIZED ONE

- China provides a good example: official Chinese statistics place the number of internal migrants over the past 20 years at over 10% of the 1.3bn population. 45% were aged 16-25 and two-thirds were male. Urban incomes are around 3.5 times those of rural workers.
- A Marxist criticism states that profits will be retained by the capitalist entrepreneur, at the expense of workers. In addition, urban expansion might be driven by increases in capital rather than labour.
- Evidence suggests that surplus labour is as likely in the urban sector as in the agricultural sector. Migrating workers may possess insufficient information about job vacancies, pay and working conditions. This results in high unemployment levels in towns and cities.
- Towns and cities may also be fixed in size and unable to accommodate large numbers of immigrants. This gives rise to slums and shanty towns, which are often illegal, built on flood planes or areas vulnerable to landslides and without sanitation or clean water. Cape Town provides a good example. Globally 1bn people live in slums.

PATTERNS OF DEMAND THEORY

- Chenery's model defines economic development as a set of interrelated changes in the structure of an underdeveloped economy that are required for its transformation from an agricultural economy into an industrial economy for continued growth in addition to accumulation of capital both human and physical.
- Chenery's model requires an altering of the existing structures within an underdeveloped economy to pave way for the penetration of new industries and modern structures to attain the status of an industrial nation. It is quite similar to Lewis' model but in its opinion investment and savings although necessary are not enough to drive the degree of growth that is required. Chenery's model adopts four main strategies to achieve economic growth:
  - Transformation of production from agricultural to industrial production
  - Changing composition of the consumer demand from emphasis on food commodities and other consumables to desire for multiple manufactured goods and services
  - International trade; creating a market for its exports
  - Using resources as well as changes in socio-economic factors as the distribution of the country's population.

LIMITATIONS

- One of the criticisms against the Chenery's structural change model is that it shortchanges critical valuables judgement.
- Again, in his analysis of Chenery's theory, Krueger identified areas of market failure emanating from exploitation of static comparative advantage inferior for less developed countries to a more protective or interventionist approach which merely focuses on producing dynamic comparative advantages. This observation bears some relevance to the protection mechanism established under the 'Common Exchange Tariff (CET)' mechanism for ECOWAS member countries. Here, there is clause in the CET that allows Nigeria to use tariffs to protect some local industries
- In spite of these limitations, Chenery's model is useful for economic growth where different countries with varying economic systems are able to support each other in terms of economic relations. On this note, this model suits the economic development efforts of developing countries against the backdrop of globalization

NEO-COLONIAL DEPENDENCE MODEL

- The neocolonial dependence model is basically a **Marxist approach**.
  - Underdevelopment is due to the historical evolution of a highly unequal international capitalist system of rich country-poor country relationships.
  - Developed nations are intentionally exploitative or unintentionally neglectful towards developing countries. Underdevelopment is thus externally induced.
  - Developing countries are destined to be the sweatshops of the rich nations (through their multinationals for example) and depend on developed nations for manufacturing goods that are high-value-added.

Many developing countries were forced to become exporters of primary commodities by their colonial masters. Many of these countries still depend on primary commodities after independence. However, with average prices of primary commodities falling substantially (by half in many cases) since 1950s, dependence on primary commodities export is impoverishing to these countries. The economies of Zambia and Nigeria had been negatively affected by falling prices for their commodities exports. However, countries like Thailand and Malaysia who used to depend heavily on tin, rubber and palm oil are able to diversified into manufacturing exports. These countries went on to develop strong manufacturing sector.

FALSE PARADIGM MODEL

- underdevelopment is due to faulty and inappropriate advice provided by well-meaning but often uninformed, biased, and ethnocentric international (often western) expert advisers to developing countries.
- IMF and World Banks took a lot of blame from the advocators of this model. Joseph Stiglitz in Making Globalization Works and Jeffrey Sachs in The End of Poverty documented some cases where inappropriate advices were given by expert advisers from developed countries to developing nations.
- If the advice of these international advisers were helpful they usually benefit the urban elites. Some economists argue that loans provided to developing countries in the 1960s and 1970s contribute to debt crisis in some developing countries in the 1980s.

An Case of Misdirection. *Eucalyptus is a fast growing tree in favorable conditions and its wood has good commercial value. Encouraged by international advisers, this tree was introduced to many parts of India indiscriminately in the 1970s. In Bangalore, a dry zone, yields were only 20% of the projected figure by the government. In Western Ghats, eucalyptus plantations were taken up on a large scale by clear-felling of excellent rainforest. Unfortunately, these eucalyptus trees were attack by fungus called pink disease and rendered the plantation useless. The losers in this case were the local Indian farmers and environmental quality of India.*

THE DUALISTIC DEVELOPMENT THEORIES

- This thesis recognizes the existence and persistence of increasing divergences between rich and poor nations, and between rich and poor people at various levels. The urban elites in developing countries will remain rich and become richer. The wealth of these elite will not trickle down to the rest of the society. According to the World Bank, the average for the richest twenty countries in the world was 15 times the average for the poorest twenty countries in 1960, and in 2000 it is 30 times — twice as high.
- However, case studies of Taiwan, South Korea, China, Costa Rica, Sri Lanka, and Hong Kong demonstrated that higher income levels can be accompanied by falling and not rising inequality. The inverted Kuznet Curve shows that as income per capita continues to increase inequality of income can be reduced.
- Basically, dependency theories highlight the need for major new policies to eradicate poverty, to provide more diversified employment opportunities, and to reduce income inequalities. The Marxist approach to growth would recommend nationalization of industries that are controlled by foreign companies (especially those from the western colonists and multinationals) and implement state-run production to reduce foreign controls on local economy.

DEPENDENCY THEORIES

- Dependency theories offer little explanation for economic growth and sustainable development. They tell us little on how to obtain economic growth.
- The actual economic experience of developing countries that pursued nationalization and introduced state-run production had been mostly negative. Nationalized companies were usually badly managed. Consequently, the operations were inefficient and productivity fell. Falling output led to falling export earnings. This was bad news for growth.

NEOCLASSICAL GROWTH MODEL

- Neoclassical Growth Model owed its origin to Robert Solow (in 1956) and Trevor Swan (in 1956). The neoclassical growth model says that grow due to increased capital stock as in Harrod-Domar Model can only be temporary because capital is subjected to diminishing marginal returns. The economy can achieve a higher long-run growth path only with a grow in labor supply, labor productivity or capital productivity. Variation in growth rate is explained by difference in the rate of technological change which affects labor and capital productivity. Advances in technology however is independent of the rate of investment, that is technology is exogenous to the model.
- In the 1980s, Reaganomics and Thatcherism were the buzzwords. These policies recommended small government with little government intervention in the market, reduced distortions in the market, promoted free markets, encouraged competition and regarded multinationals in favorable lights.
- Underdevelopment is seen as the product of poor resource allocation, incorrect pricing policies and too much state interventions that cause market distortion.
- The answer is promotion of free markets and laissez-faire economics through privatization and deregulation.
- Governments should also have market-friendly approaches to address externality problems. Governments should invest in physical and social infrastructure, health care facilities, education and provide suitable climate for private enterprises. Governments should also be friendly towards multinationals and attract Foreign Direct Investment (FDI) as this policy brings injection into the economy.

NEOCLASSICAL GROWTH MODEL

Criticisms:

- Economic growth does not means development. Policies that promote economic growth may benefit the rich in the expense of the poor and the environmental qualities (more environmental degradation). A smaller government could also mean less social facilities for the poor.
- South Korea, Singapore, Japan, and China do not have genuine free market economies but are economic success stories. In fact, governments in these countries play active roles in directing their respective economies.
- Solow-Swan Model suggests that low capital to labor ratio in developing countries means that the rate of return on investment is high but this is not supported by historical data.
- The residual in Solow-Swan Model which is attributed to technology only explains 50% of historical growth in developed nations. There is much room for improvement in this model.

ENDOGENOUS GROWTH MODEL

- This model is called Endogenous growth model because it makes technology a part of the model and not as a residual. This model tries to explain the rate of technological change.
- Persistent economic growth is determined by the system governing the production process as technology is now part of the model. Economic growth is a natural consequence of long run equilibrium.
- The model allows potentially increasing return to scale from higher level of capital investment, especially investment that has positive externalities. Capital is expanded to encompass human capital .
- Human productivity could increase due to higher skill attainment and learning-by-doing. The latter suggests that experience allows a worker to have higher productivity.
- Human capital can be encouraged through education and skill-training programmers.
- The rate of technological change can increase due to higher investment in R&D. R&D may also confer positive externality to knowledge-intensive industries.
- Protection of intellectual property rights is important because this legal monopoly gives incentive to carry out R&D.
- The model implies an active role for government to promote human capital formation (through education, better access to health care, and better nutrition) and encourage knowledge-intensive industries. To achieve the latter, some government even took the trouble to pick future industrial winners. Japan in the past promoted chemical and heavy-industry. More recently it promoted biochemical industry. Malaysia, for example, established a whole new town called Cyberjaya to attract knowledge-intensive industries and R&D into the country.

- **Criticisms**:
  - Developing countries cannot take full advantage from the recommendation of this model that is based on neoclassical principles of efficient free market because of poor infrastructure, inadequate institutional structures, and imperfect capital and good markets. Many developing countries, for instance, do not have adequate protection for intelligent property rights and insurance markets that encourage entrepreneurship.
  - The model fails to explain why low-income countries where capital is scarce have low rates of factory capacity utilization.

WORLD ECONOMICS:

MODERN FACTORS OF ECONOMIC GROWTH AND ECONOMIC DEVELOPMENT

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FACTORS THAT AFFECT ECONOMIC GROWTH

1. **Natural Resources**. The discovery of more natural resources like oil, or mineral deposits may boost economic growth as this shifts or increases the country's Production Possibility Curve. Other resources include land, water, forests and natural gas. Realistically, it is difficult, if not impossible, to increase the number of natural resources in a country. Countries must take care to balance the supply and demand of scarce natural resources to avoid depleting them. Improved land management may improve the quality of land and contribute to economic growth.

2. **Physical Capital or Infrastructure.** Increased investment in physical capital such as factories, machinery, and roads will lower the cost of economic activity. Better factories and machinery are more productive than physical labor. This higher productivity can increase output. For example, having a robust highway system can reduce inefficiencies in moving raw materials or goods across the country which can increase its GDP.

3. **Population or Labor.** A growing population means there is an increase in the availability of workers or employees, which means a higher workforce. One downside of having a large population is that it could lead to high unemployment.

FACTORS THAT AFFECT ECONOMIC GROWTH

4. **Human Capital.** An increase in investment in human capital can improve the quality of the labor force. This would result in an improvement of skills, abilities, and training. A skilled labor force has a significant effect on growth since skilled workers are more productive.
5. **Technology.** Another influential factor is the improvement of technology. Technology could increase productivity with the same levels of labor, thus accelerating growth and development. This means factories can be more productive at lower costs. Technology is most likely to lead to sustained long-run growth.
6. **Law.** An institutional framework which regulates economic activity such as rules and laws. There is no specific set of institutions that promote growth.

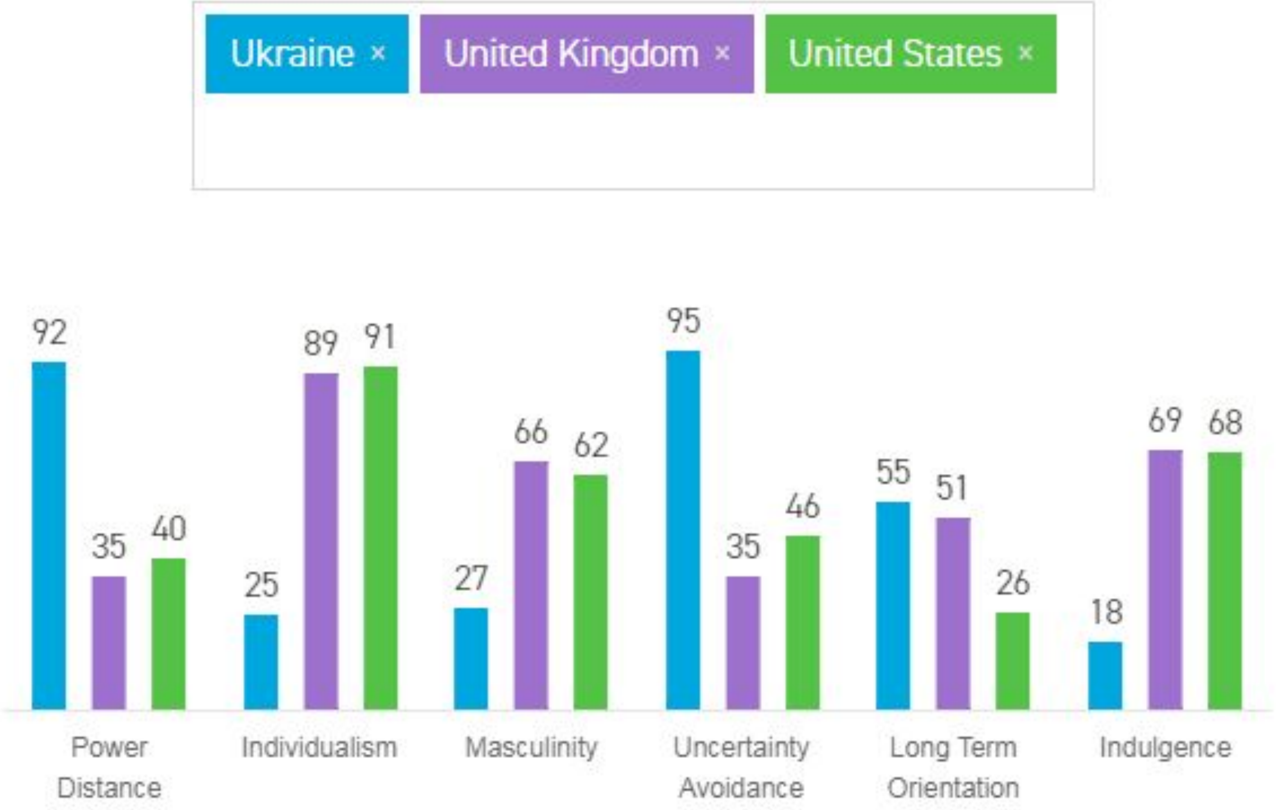
FACTORS THAT LIMIT ECONOMIC GROWTH

1. **Poor health and low levels of education**. People who don't have access to healthcare or education have lower levels of productivity. This means the labor force is not as productive as it could be. Therefore, the economy does not reach the productivity it could otherwise.
2. **Lack of necessary infrastructure**. Developing nations often suffer from inadequate infrastructures such as roads, schools, and hospitals. This lack of infrastructure makes transportation more expensive and slows the overall efficiency of the country.
3. **Flight of Capital**. If the country is not delivering the returns expected from investors, then investors will pull out their money. Money often flows out the country to seek higher rates of returns.
4. **Political Instability**. Similarly, political instability in the government scares investors and hinders investment. For example, Zimbabwe has been plagued with political uncertainty and laws favoring indigenous ownership. This has scared off many investors who prefer smaller but surer returns elsewhere.
5. **Institutional Framework**. Often local laws don't adequately protect rights. Lack of an institutional framework can severely impact progress and investment.

FACTORS OF ECONOMIC GROWTH

- **Boom and Bust Business Cycles.** If economic growth is high-speed and inflationary, then the level of growth will become unsustainable. This could lead to a recession like the Great Recession in 2008. However, this type of growth is typical of a business cycle.
- **Export-led.** The Japanese and Chinese economy have experienced export-led growth thanks to a high current account surplus. This is because they have significantly more exports than imports.
- **Consumer.** The US economy is dependent on consumer spending for economic growth. As a result, they also have a higher current account deficit.
- **Commodity exports**. These economies are dependent on their natural resources like oil or iron ore. For example, Saudi Arabia has a had a very prosperous economy thanks to their oil exports. However, this can cause a problem when commodity prices fall, and there aren't other industries to balance things out.

HOFSTEDE-INSIGHTS



1. Power Distance is defined as the extent to which the less powerful members of institutions and organizations within a country expect and accept that power is distributed unequally.
2. The fundamental issue addressed by this dimension is the degree of interdependence a society maintains among its members.
3. The fundamental issue here is what motivates people, wanting to be the best (Masculine) or liking what you do (Feminine).
4. The extent to which the members of a culture feel threatened by ambiguous or unknown situations and have created beliefs and institutions that try to avoid these is reflected in the score on Uncertainty Avoidance.
5. This dimension describes how every society has to maintain some links with its own past while dealing with the challenges of the present and future, and societies prioritise these two existential goals differently.
6. This dimension is defined as the extent to which people try to control their desires and impulses, based on the way they were raised.

PATH DEPENDENCY

- Path dependency is an idea that tries to explain the continued use of a product or practice based on historical preference or use. This holds true even if newer, more efficient products or practices are available due to the previous commitment made. Path dependency occurs because it is often easier or more cost effective to simply continue along an already set path than to create an entirely new one.
  - *An example of path dependency would be a town that is built around a factory. It makes more sense for a factory to be located a distance away from residential areas for various reasons. However, it is often the case that the factory was built first, and the workers needed homes and amenities built close by for them. It would be far too costly to move the factory once it has already been established, even though it would better serve the community from the outskirts of town.*

MIDDLE CLASS

- Different, partly overlapping concepts of ‘class’
  - Statistical partitioning of distribution in discrete, partly arbitrary, groups
  - Sociological perspective (position in division of labour, occupations, education)
  - Political (capacity to forge identities and articulate common demands)

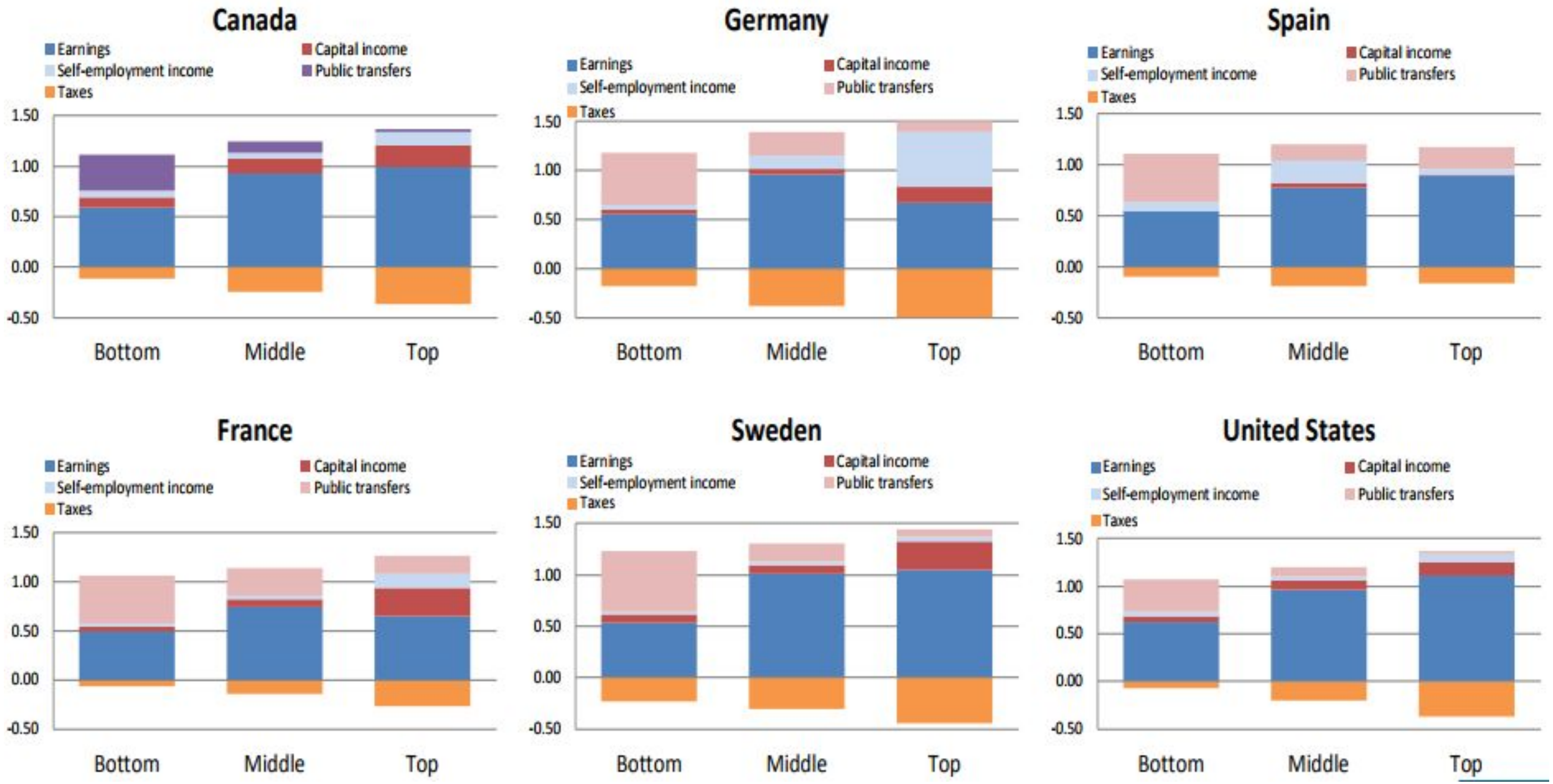
'Middle Class'

Middle class is a description given to individuals and households who fall between the working class and the upper class within a societal hierarchy. In Western cultures, persons in the middle class tend to have a higher proportion of college degrees than those in the working class, have more income available for consumption and may own property. Those in the middle class often are employed as professionals, managers and civil servants.

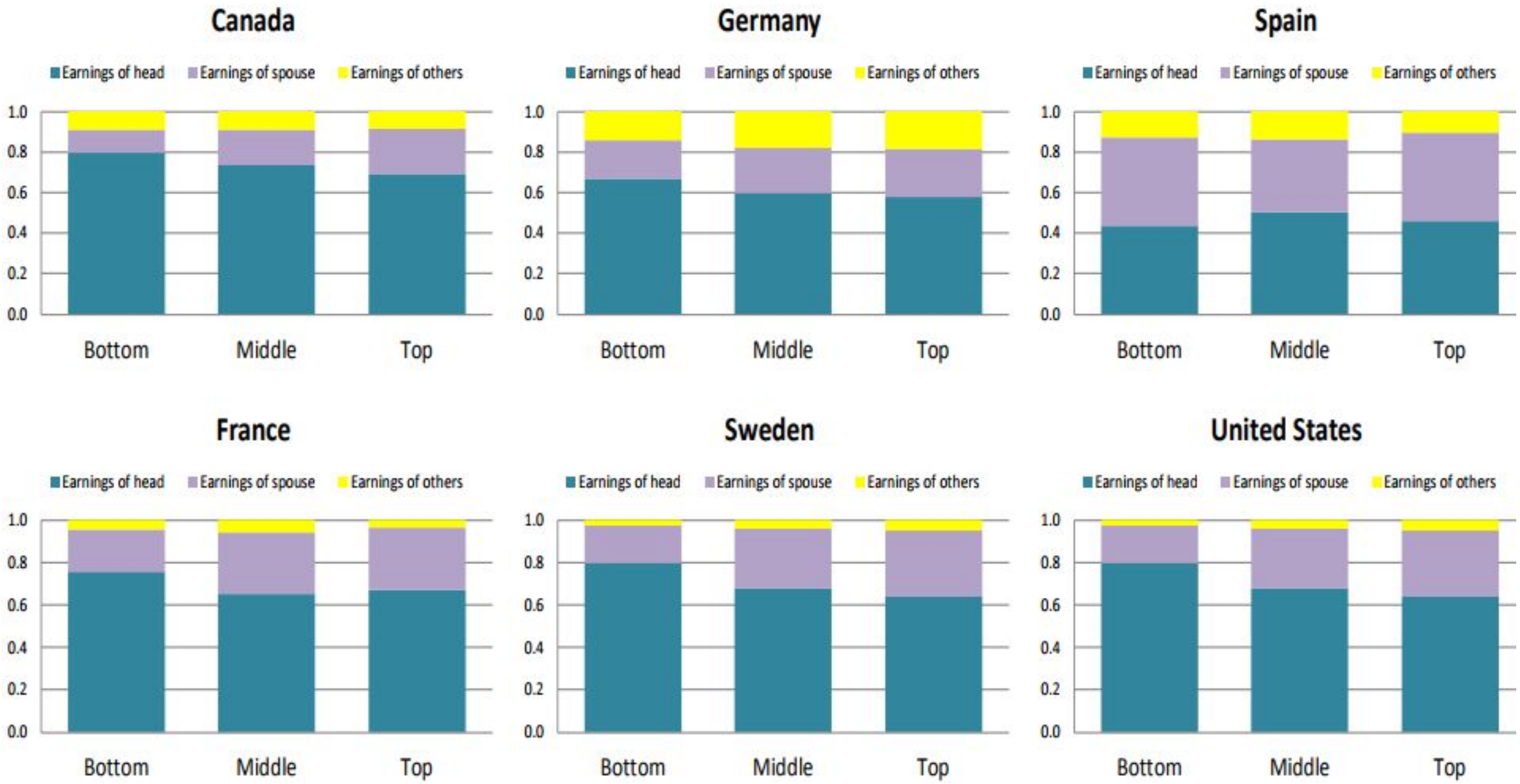
MIDDLE CLASS

- no single OECD definition of the 'middle-class' analogue that what we use for income poverty (40, 50, 60% of median household disposable income), i.e. various OECD studies used different definitions
- general definition of the middle class used here: people in 5th to 9th decile of the distribution (Palma ratio). At this stage, not much evidence that alternative definitions would lead to similar conclusions

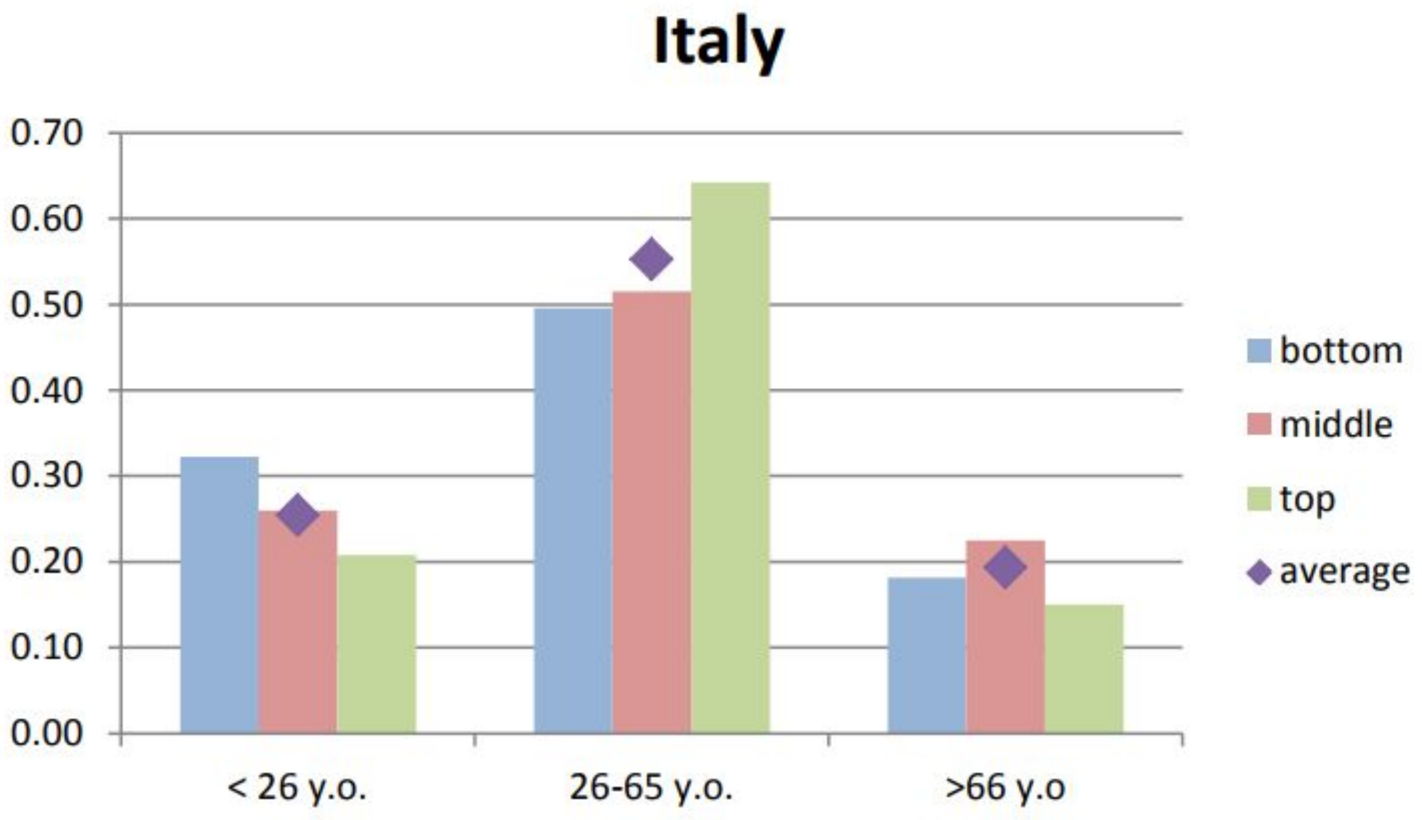
MIDDLE CLASS DEPENDS ON EARNINGS AS MAIN INCOME SOURCE



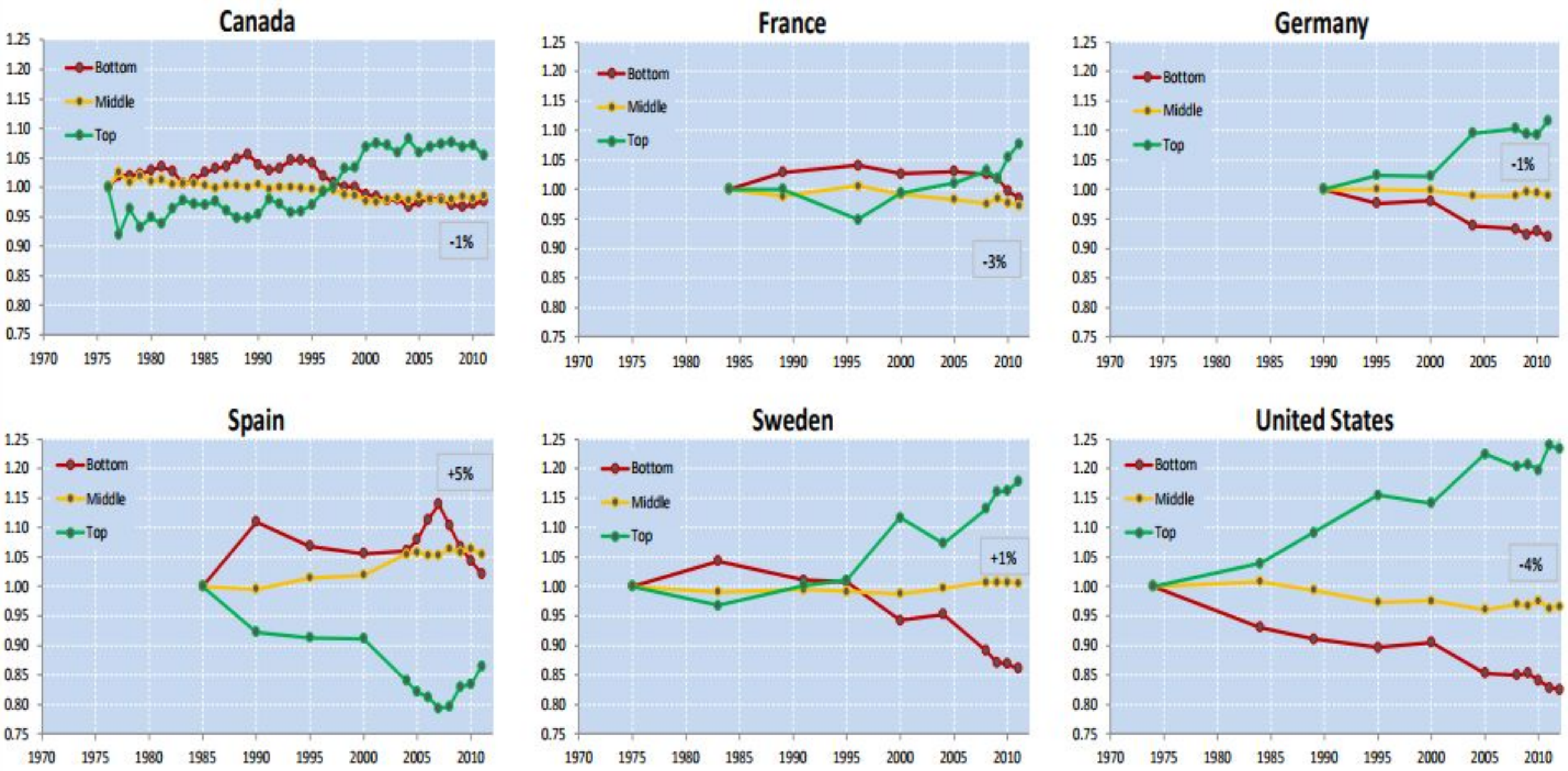
INCREASINGLY DUAL-EARNINGS HOUSEHOLDS



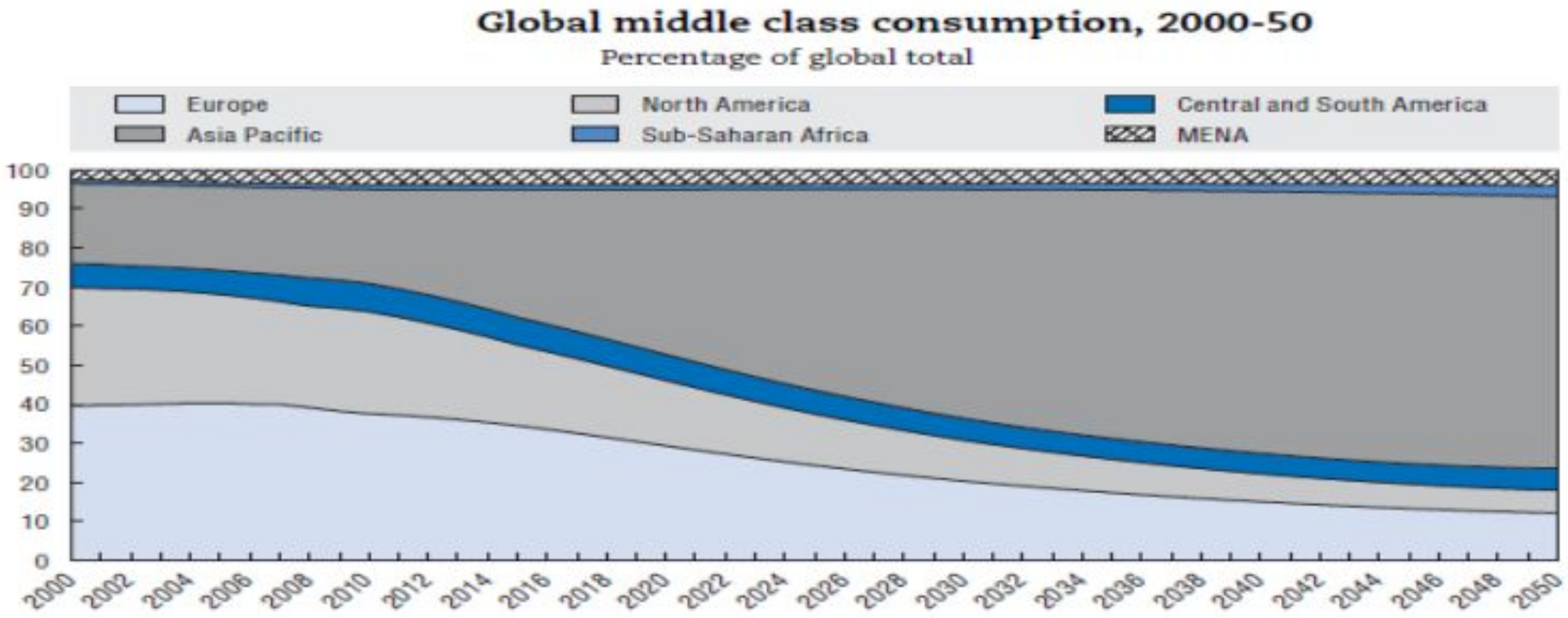
PREDOMINANTLY PRIME-AGED (WITH CHILDREN)



SIGNIFICANTLY CHANGES IN THE US (LOWER) AND SPAIN (HIGHER), SMALLER CHANGES ELSEWHERE



- ‘Middle class’ is a political construct, used to convey images of greater contiguity with upper classes that with ‘working class’: statements about the fate of the middle class immediately gain strong political attention (e.g. press debates in US, Canada, Germany, others)
- Growth of middle-classes in emerging countries, bringing with it new demands which political system are unable to answer (e.g. street protest in Israel, Brazil, Arab Spring, etc.)



FINANCIAL CRISES

The amount of subprime mortgage debt, which was *guaranteed* by **Freddie Mac** and **Fannie Mae**, continued to expand into the early 2000s, about the time the Federal Reserve Board began to cut *interest rates* drastically to fend off a **recession**. The combination of loose credit requirements and cheap money spurred a housing boom, which drove speculation, which in turn drove up housing prices.

THE GREAT RECESSION

- The Great Recession is a term that represents the sharp decline in economic activity during the late *2000s*, which is generally considered the largest downturn since the Great Depression.
- The term *Great Recession* is a play on the term *Great Depression*
- Great Recession applies to both the U.S. recession, officially lasting from *December 2007 to June 2009*, and the ensuing global recession in 2009. The economic slump began when the U.S. housing market went from boom to bust and large amounts of mortgage-backed securities and derivatives lost significant value.

BEFORE GREAT RECESSION

- The investment banks, **looking for easy profits** in the wake of the dotcom bust and 2001 recession, created collateralized debt obligations (CDOs) out of mortgages purchased on the secondary market.
- Because subprime mortgages were bundled with prime mortgages, there was no way for investors to understand the risks associated with the product.
- Around the time when the market for CDOs was heating up, the housing bubble that had been building up for several years was beginning to burst.
- As housing prices fell, subprime borrowers began to default on loans that were worth more than their homes, accelerating the decline in prices.
- When investors realized the CDOs were becoming worthless due to the toxic debt they represented, they tried to unload them, but there was no market for them.
- This caused a cascade of subprime lender failures, which created a liquidity contagion that worked its way to the upper tiers of the banking system.
- Two major investment banks, Lehman Brothers and Bear Stearns, collapsed under the weight of their exposure to the subprime debt, and more than **450 banks** failed over the next **5 years**.

DOTCOM BUBBLE

- The **dotcom bubble** occurred in the late 1990s and was characterized by a rapid rise in equity markets fueled by investments in Internet-based companies. *During the dotcom bubble, the value of equity markets grew exponentially, with the technology-dominated NASDAQ index rising from under 1,000 to more than 5,000 between 1995 and 2000.*
  - The dotcom bubble grew out of a combination of the presence of speculative or fad-based investing, the abundance of venture capital funding for startups and the failure of dotcoms to turn a profit. Investors poured money into Internet startups during the 1990s in the hope that those companies would one day become profitable, and many investors and venture capitalists abandoned a cautious approach for fear of not being able to cash in on the growing use of the Internet.

The 1990s was a period of rapid technological advancement in many areas, but it was the commercialization of the Internet that led to the greatest expansion of capital growth the country had ever seen. Although high-tech standard bearers, such as Intel, Cisco, and Oracle were driving the organic growth in the technology sector, it was the upstart dotcom companies that fueled the stock market surge that began in 1995.

From IMF

LESSONS

- Originators need to be "incentivized" to make loans to high-quality borrowers and to monitor loan performance more carefully.
- The governance structure of the risk management system needs to be improved in financial firms in which the incentives are biased toward returns rather than the risks involved in attaining them.
- The incentives to use credit rating agencies and the incentive structures within credit rating agencies themselves need to be reexamined
- Investors need to perform their own due diligence and ask the right questions about the riskiness of the securities they are purchasing

EIU GLOBAL FORECAST - HIGHER INTEREST RATES ARE COMING

- The US economy will continue to motor along; the euro area will absorb more of labour market slack; the Chinese government will manage its economic slowdown carefully; and Japan's economy will grow by 1.5%.
- Higher commodity prices will prove a fillip for emerging-market exporters, as will strong external demand from developed markets.
- However, 2018 will also be characterised by tightening monetary policy and credit conditions. On balance, the global economy is forecast to expand by 3% in 2018 and 2.9% in 2019, from an estimated 3% in 2017.

DEVELOPED WORLD

- The US economy is in good shape, and we have revised up economic growth in 2018 to 2.5%, from 2.3% previously. Wage growth is showing signs of accelerating, and the unemployment rate is at its lowest level since 2000.
- Expects the US economy to show signs of overheating in the next two years, as a result of which the Fed will quicken the pace of monetary tightening, especially given the recent tax changes. Unable to cope with this, the economy will face a downturn in early 2020.
- The recent revival of the euro zone economy is likely to be sustained, but political risk will remain high. EU leaders are currently boosting the region's resilience to shocks, in part by renewing their push for further integration of the economic and monetary union.
- A decision on reform proposals will be made at the EU summit in June 2018. Following the renewed landslide secured by the ruling Liberal Democratic Party (LDP) in Japan, Shinzo Abe is in a strong position to secure another term as LDP leader when the party votes in late 2018. This comes in the context of the country's mild economic recovery under the prime minister's recovery plan.

EMERGING MARKETS

- Conditions for emerging markets to become more challenging in the first half of the forecast period as US interest rates continue to rise. India will be Asia's fastest-growing large economy in 2018-22, expanding at an average annual rate of 7.9%. Growth will also remain on track in the Association of South-East Asian Nations (ASEAN) member states, with an average annual expansion of 4.8%. Vietnam, Cambodia and Myanmar, in particular, will continue to record growth rates above 6%, owing to relatively low wage costs and advantageous geographic locations.
- the Chinese economy to slowly slightly in 2018, to 6.4%, from an estimated 6.9% in 2017. The government's long-held target of doubling real GDP between 2010 and 2020 is within its grasp; it requires annual average GDP growth of 6.3% in 2018-20. We believe that it will meet this target without requiring significant economic stimulus. We expect China to move away from GDP targeting in the next decade. This is ideologically consistent with the call of the president, Xi Jinping, for more inclusive growth in his landmark speech at the party congress at the end of 2017. As such, we expect growth to continue to slow steadily in the forecast period, reaching 5.2% in 2022.

EMERGING MARKETS

- The ongoing economic recovery in Latin America is forecast to gather momentum in 2018-19, after several years dominated by macroeconomic policy adjustments to the end of the commodities boom of the previous decade. Sustained Chinese growth will continue to provide a favourable external environment for the region, particularly for commodity exporters such as Brazil and Argentina. This, combined with a rise in global risk appetite, as reflected in lower sovereign credit default swap rates (except for Venezuela, which defaulted on some external debt obligations in late 2017, taking the country further into economic and financial crisis), has generated strong growth in local stockmarkets.
- At present, seven countries in the Middle East that collectively account for a quarter of the regional population are either torn by civil war or destabilised by Shia-Sunni rivalry. Geopolitical risk has also risen rapidly within the Gulf Co-operation Council (GCC). We expect the boycott of Qatar by some of the GCC countries and Egypt to continue until at least 2021. In this period divisions will harden between Qatar, Turkey and Iran on one side, and Saudi Arabia, the UAE and Egypt on the other. The long-term rivalry between Saudi Arabia and Iran is likely to destabilise a group of other countries in the Middle East, including Iraq, Syria, Lebanon and Yemen. Tensions are likely to increase rather than diminish in the region in the coming months.
- Following a dismal performance in Sub-Saharan Africa over 2016-17, we expect a lacklustre recovery to take hold from 2018. This will be driven by a favourable external environment as export prices strengthen and trade gathers pace. However, policy mismanagement, unsupportive political dynamics and gradual tightening of credit conditions in developed economies will weigh on future prospects. On balance, the region is forecast to grow by 3.3% a year in 2018-22.

EXCHANGE RATES

- The US dollar has continued to depreciate in early 2018, in spite of solid economic data, major tax reform and a clear commitment by the Fed to raising interest rates. Previously, markets did not believe monetary tightening by the Fed to be credible.
- However, this changed in early February when global stockmarkets fell sharply in response to suggestions of faster US wage growth. Regular interest-rate increases should provide the dollar with fresh support over the next two years, but any rally in 2018-19 will be modest at most. Among G10 currencies, the euro made the biggest gains against the dollar in 2017 as economic data went from strength to strength and some political risk receded. Further supporting the currency, the ECB is slowly becoming more upbeat in its communication.
- However, we believe that the first interest-rate rise is still two years away, and the euro zone continues to face considerable political challenges, which will limit economic momentum. On balance, we expect the euro to hold steady against the dollar in 2018-19. The yen is expected to appreciate further against the dollar in 2018-19 owing to its safe-haven appeal, and as the BOJ slows the pace of its asset purchases over dwindling bond-market liquidity concerns

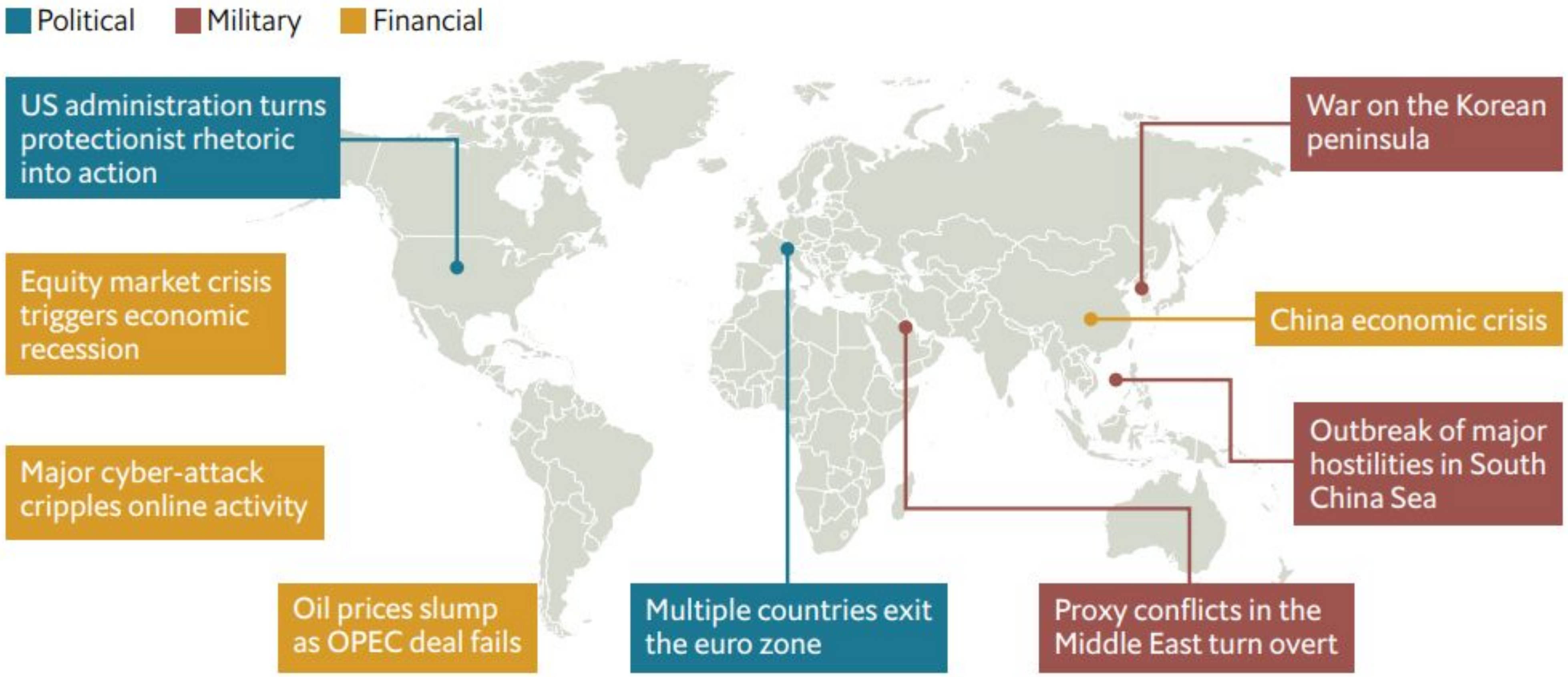
COMMODITIES

- The price of crude oil is likely to remain range-bound, at US$60-70/barrel in 2018-19 for dated Brent Blend, despite the efforts of OPEC and its partners, notably Russia, to constrain global supply by extending the existing production-cut deal until the end of 2018. These efforts will be largely offset by US shale, which will provide both a price ceiling and a floor.
- Industrial raw materials prices are set to rise for a second successive year in 2018 on the back of strong growth in China and strict environmental controls restricting supply. We expect marginal growth in food, feedstuffs and beverages prices, reflecting rising population, incomes and rapid urbanisation.

WORLD ECONOMY: FORECAST SUMMARY

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Real GDP growth (%)										
World (PPP* exchange rates)	**3.4**	**3.6**	**3.4**	**3.2**	**3.7**	**3.8**	**3.8**	**3.5**	**3.8**	**3.8**
World (market exchange rates)	**2.4**	**2.8**	**2.8**	**2.3**	**3.0**	**3.0**	**2.9**	**2.4**	**2.8**	**2.8**
US	1.7	2.6	2.9	1.5	2.3	2.5	2.3	0.8	1.9	1.8
Euro area	-0.2	1.4	2.0	1.8	2.5	2.2	1.9	1.7	1.7	1.7
Europe	0.8	1.9	2.0	1.8	2.6	2.3	2.0	1.8	1.9	1.9
China	7.8	7.3	6.9	6.7	6.9	6.4	6.3	6.2	5.5	5.2
Asia & Australasia	4.6	4.1	4.3	4.1	4.5	4.3	4.4	4.0	4.2	4.2
Latin America	2.8	1.4	0.5	-0.5	1.2	2.1	2.3	2.4	2.8	2.8
Middle East & Africa	2.2	2.7	2.4	4.2	2.2	2.8	3.3	3.5	3.9	4.1
Sub-Saharan Africa	4.8	4.5	3.0	1.0	2.3	2.9	2.9	2.9	3.6	4.0
World inflation (%; av)	**3.8**	**3.5**	**3.2**	**3.8**	**4.5**	**5.3**	**4.4**	**3.1**	**3.1**	**3.1**
World trade growth (%)	**3.3**	**3.1**	**2.3**	**2.3**	**4.6**	**4.3**	**3.9**	**2.8**	**3.8**	**3.7**
Commodities										
Oil (US$/barrel; Brent)	108.9	98.9	52.4	44.0	54.4	63.0	60.0	57.8	60.6	63.3
Industrial raw materials (US$; % change)	-6.8	-5.1	-15.2	-2.2	20.2	5.7	-0.2	-4.7	1.0	-1.7
Food, feedstuffs & beverages (US$; % change)	-7.4	-5.2	-18.7	-3.5	-0.9	0.9	2.8	1.8	0.7	1.6
Exchange rates (av)										
¥:US$	97.56	105.86	121.02	108.76	112.14	111.26	109.06	104.00	100.00	100.20
US$:€	1.33	1.33	1.11	1.11	1.13	1.20	1.18	1.21	1.21	1.24

Global risk scenarios



WORLD ECONOMICS: MICROFINANCE

Prof. Zharova Liubov

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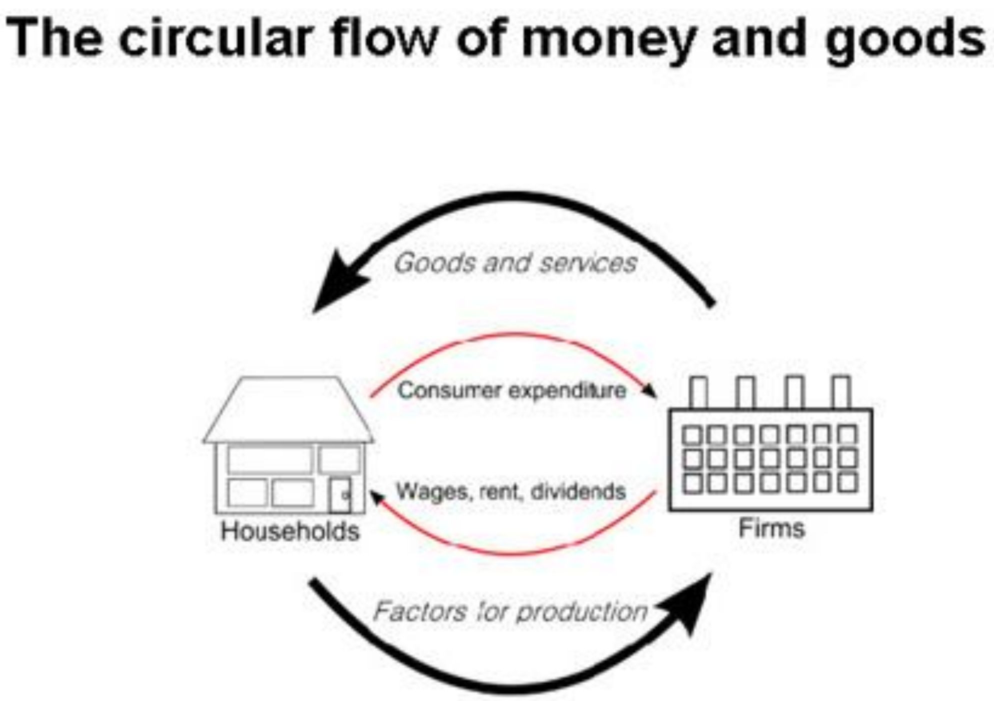
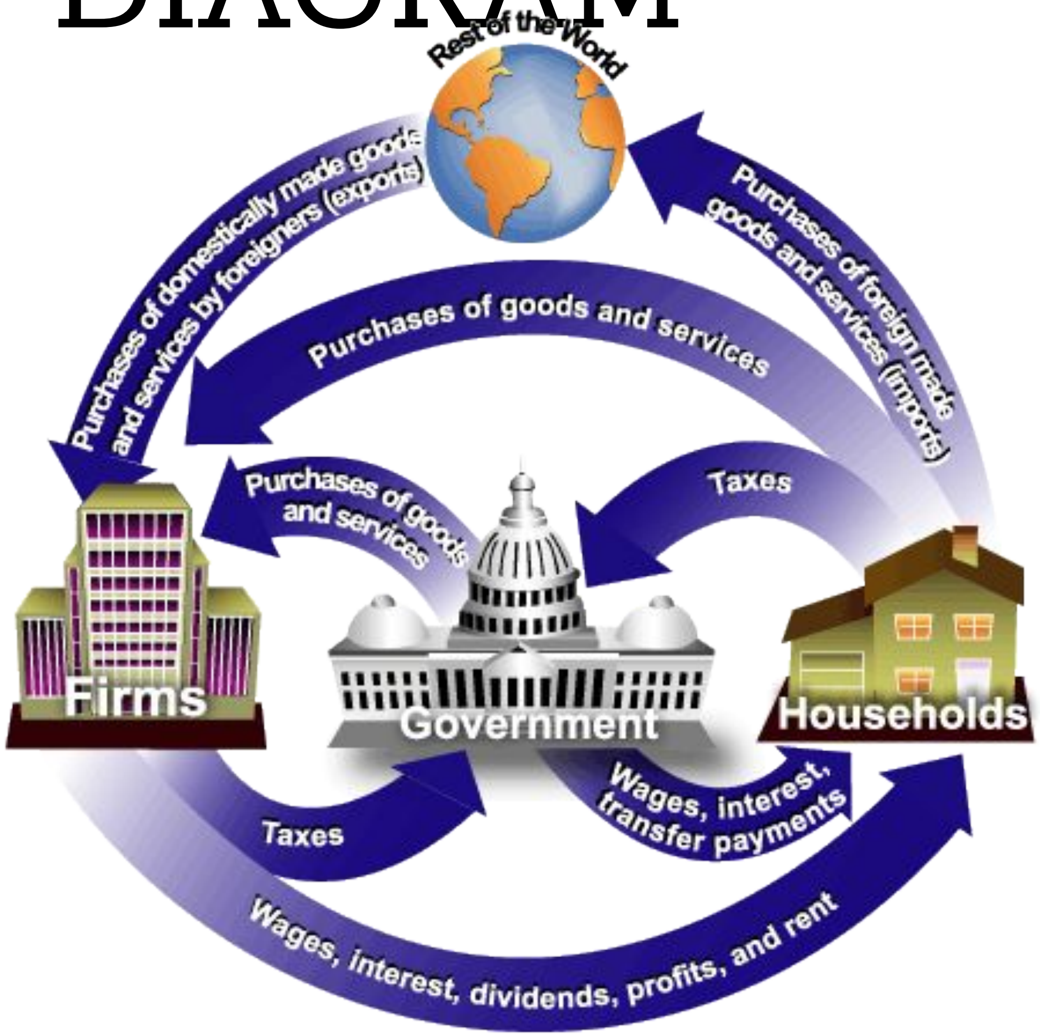
INTRO

- **MICROFINANCE**
  - Social impact of Banks;
  - basic mechanism of capital accumulation;
  - public and private investments;
  - human development index (HDI);
  - development indicators

CIRCULAR FLOW DIAGRAM





MIDDLE CLASS

- Different, partly overlapping concepts of 'class'
  - Statistical partitioning of distribution in discrete, partly arbitrary, groups
  - Sociological perspective (position in division of labour, occupations, education)
  - Political (capacity to forge identities and articulate common demands)

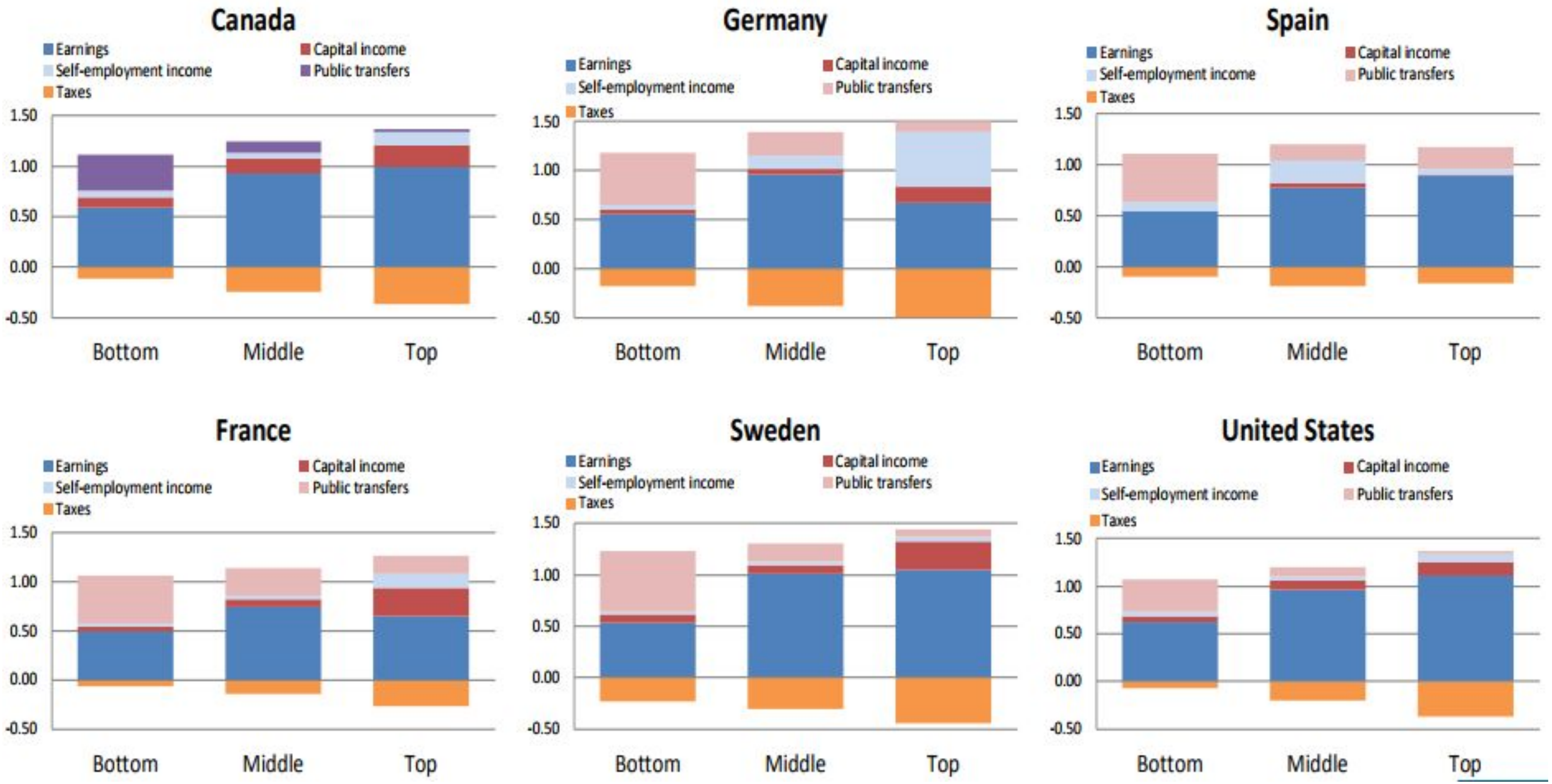
'Middle Class'

Middle class is a description given to individuals and households who fall between the working class and the upper class within a societal hierarchy. In Western cultures, persons in the middle class tend to have a higher proportion of college degrees than those in the working class, have more income available for consumption and may own property. Those in the middle class often are employed as professionals, managers and civil servants.

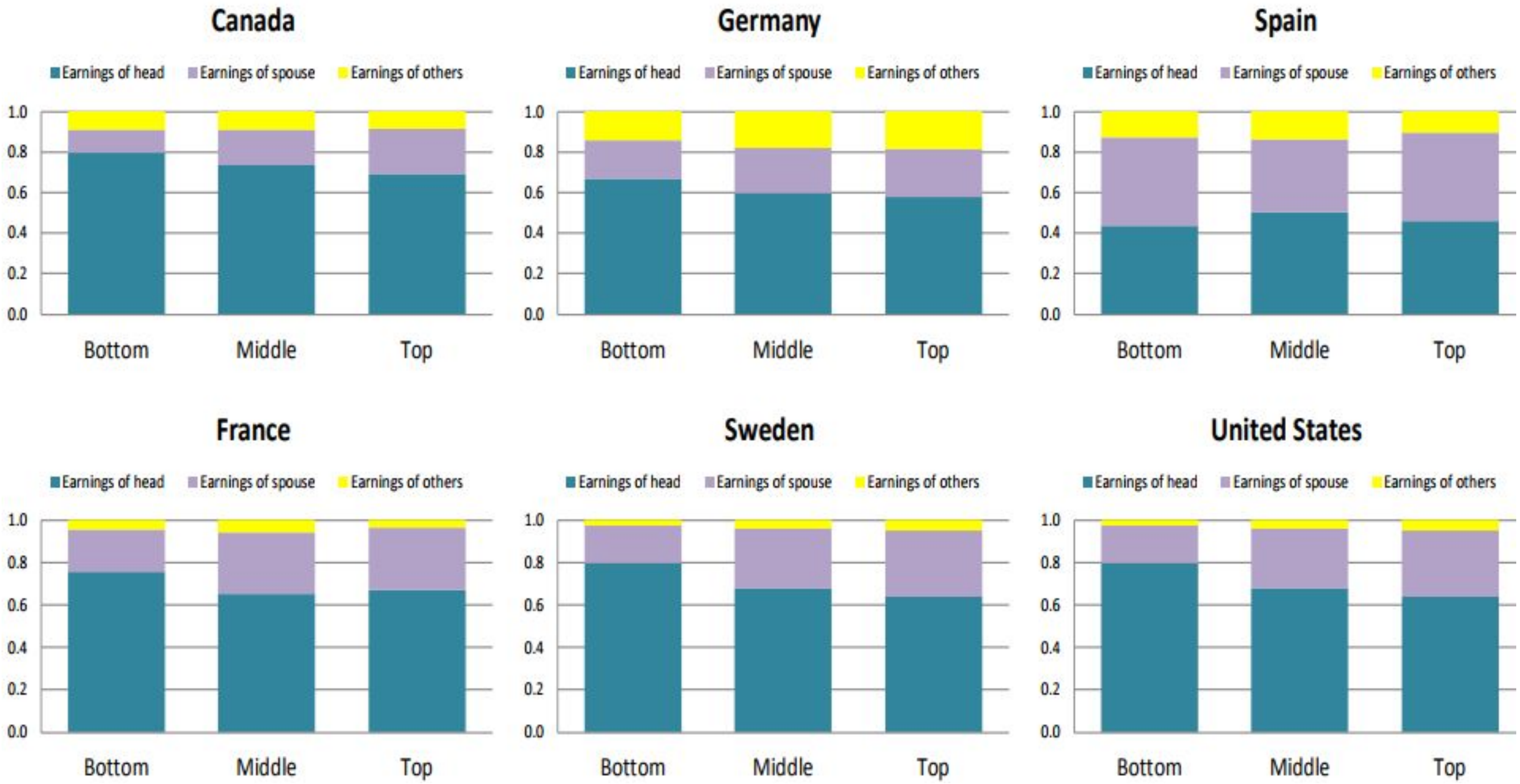
MIDDLE CLASS

- no single OECD definition of the 'middle-class' analogue that what we use for income poverty (40, 50, 60% of median household disposable income), i.e. various OECD studies used different definitions
- general definition of the middle class used here: people in 5th to 9th decile of the distribution (Palma ratio). At this stage, not much evidence that alternative definitions would lead to similar conclusions

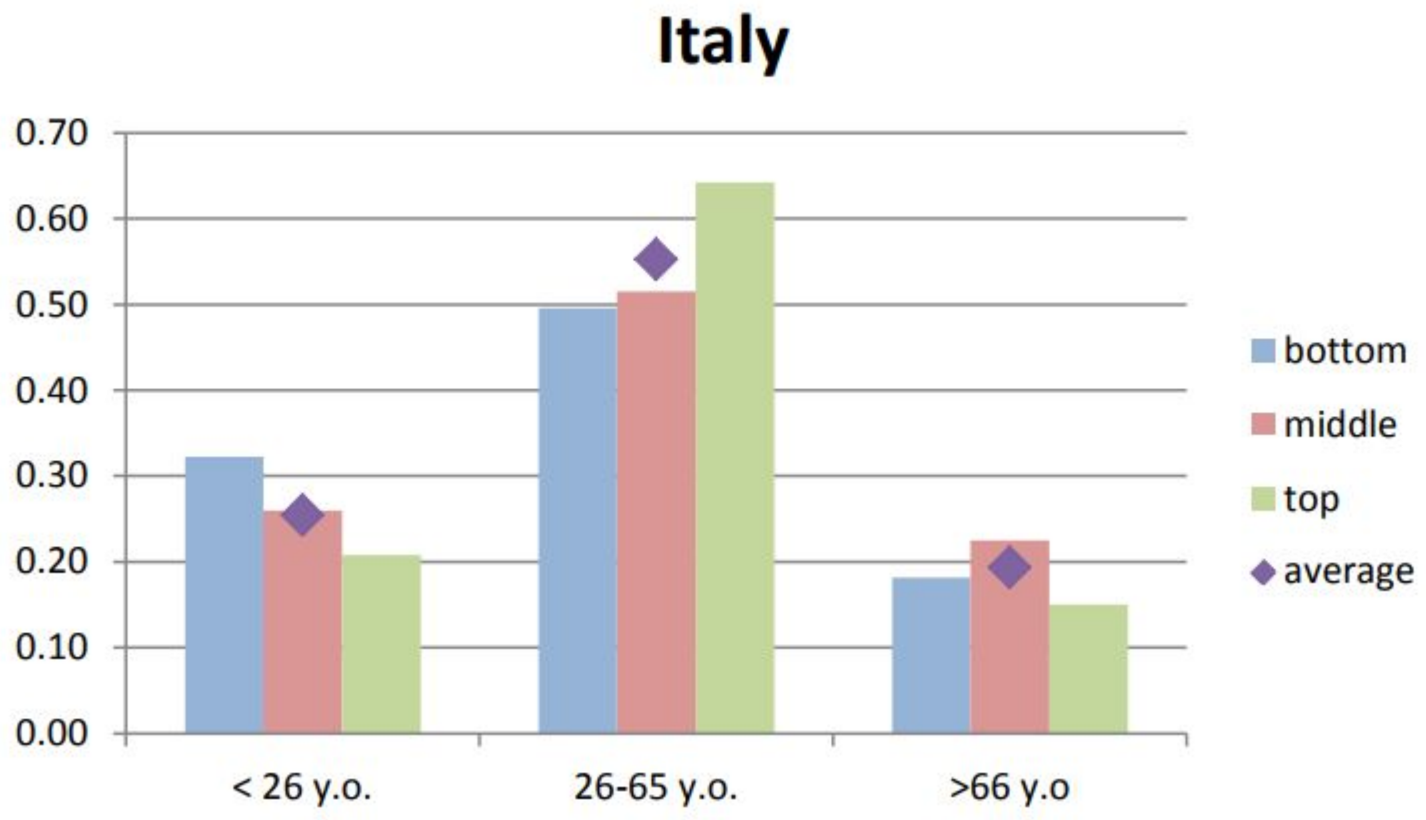
MIDDLE CLASS DEPENDS ON EARNINGS AS MAIN INCOME SOURCE



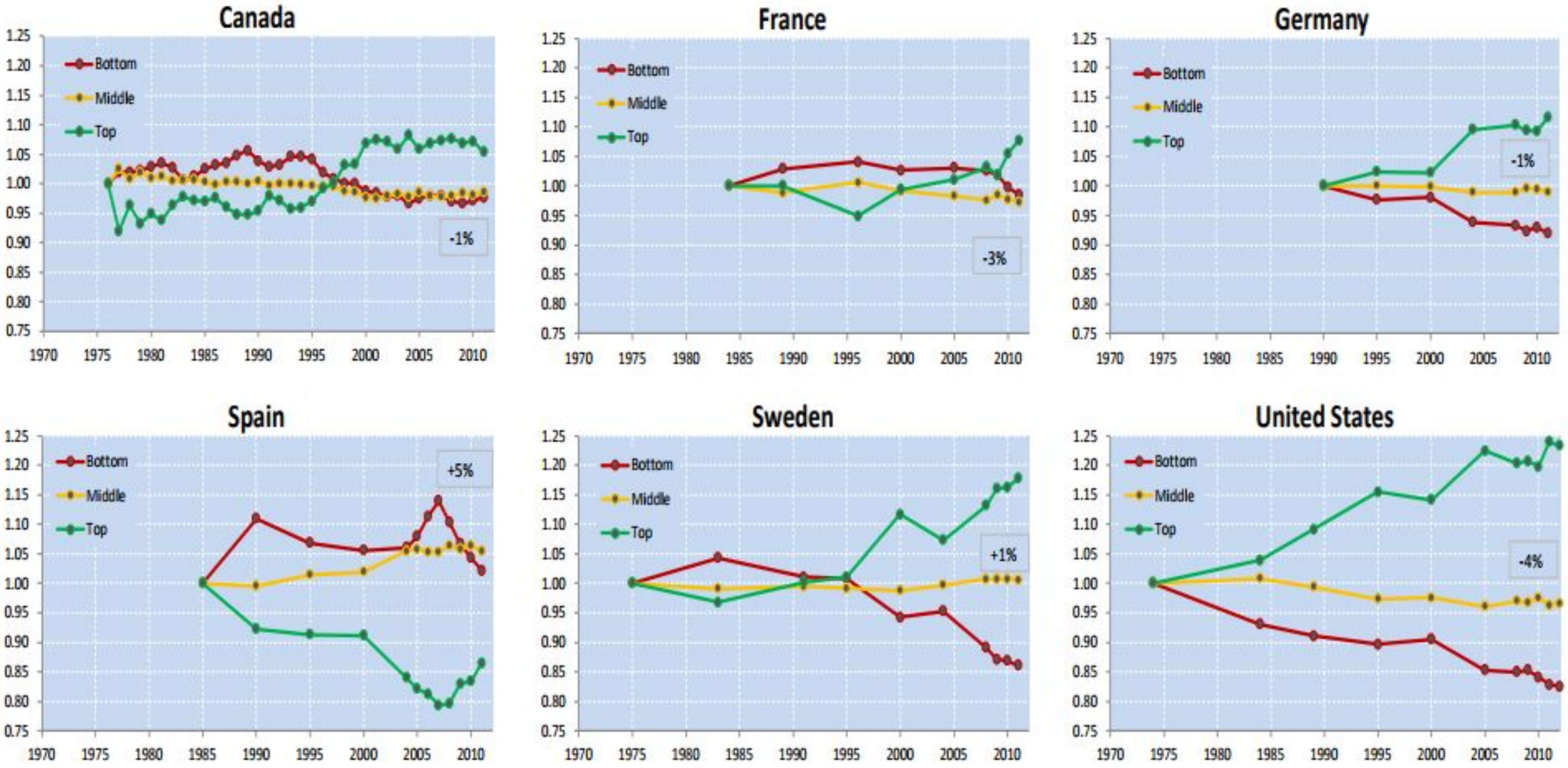
INCREASINGLY DUAL-EARNINGS HOUSEHOLDS



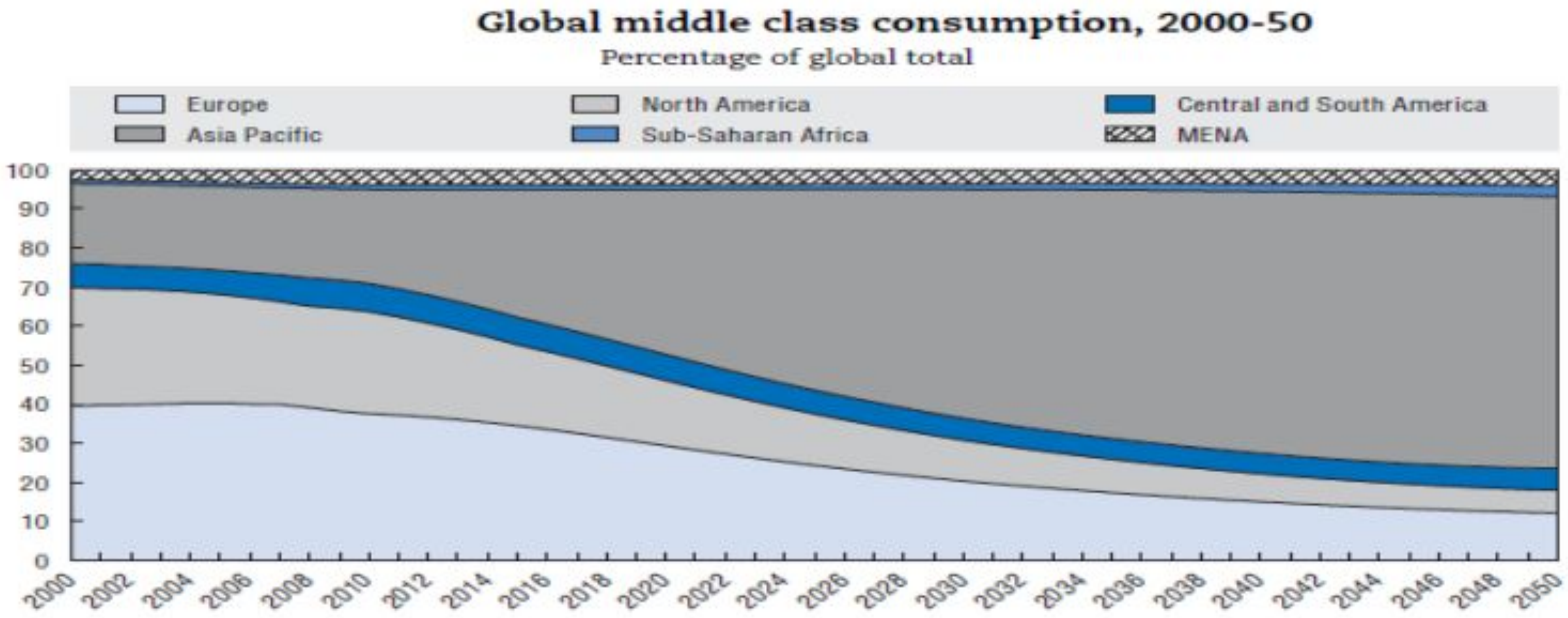
PREDOMINANTLY PRIME-AGED (WITH CHILDREN)



SIGNIFICANTLY CHANGES IN THE US (LOWER) AND SPAIN (HIGHER), SMALLER CHANGES ELSEWHERE



- ‘Middle class’ is a political construct, used to convey images of greater contiguity with upper classes that with ‘working class’: statements about the fate of the middle class immediately gain strong political attention (e.g. press debates in US, Canada, Germany, others)
- Growth of middle-classes in emerging countries, bringing with it new demands which political system are unable to answer (e.g. street protest in Israel, Brazil, Arab Spring, etc.)



CAPITAL ACCUMULATION

- Capital accumulation is a product of capital investment. Capital accumulation also increases with return from an investment. An individual or company can accumulate capital in various ways some of which include investment purchases and investment savings. Return from an investment can also lead to capital accumulation, specifically from occurrences such as investment profits, rent, interest, royalties or capital gains. Entities often increase their holdings in profitable assets to provide for greater capital accumulation. Investors can also regularly contribute to a capital base to accumulate capital and generate capital gains.

SOLOW MODEL

- **Robert Solow** developed the **neo-classical theory** of economic growth and Solow won the Nobel Prize in Economics in 1987. He has made a huge contribution to our understanding of the factors that determine the rate of economic growth for different countries.
- Growth comes from adding more **capital** and **labour** inputs and also from **ideas** and **new technology**.

WHAT ARE THE BASIC POINTS ABOUT THE SOLOW ECONOMIC GROWTH MODEL?

- The Solow model believes that a sustained rise in **capital investment** increases the growth rate only *temporarily*: because the **ratio of capital to labour** goes up.
- However, the **marginal product** of additional units of capital may decline (there are diminishing returns) and thus an economy moves back to a **long-term growth path**, with real GDP growing at the same rate as the growth of the workforce plus a factor to reflect improving productivity.
- A '**steady-state growth path**' is reached when output, capital and labour are all growing at the same rate, so output per worker and capital per worker are constant.
- Neo-classical economists believe that to raise the trend rate of growth requires an **increase in the labour supply + a higher level of productivity of labour and capital.**
- Differences in the **pace of technological change** between countries are said to explain much of the variation in growth rates that we see.
-

CATCH UP GROWTH / CUTTING EDGE GROWTH

- The Solow Model features the idea of **catch-up growth** when a poorer country is catching up with a richer country – often because a **higher marginal rate of return** on invested capital in faster-growing countries.
- The Solow model predicts some convergence of living standards (measured by per capita incomes) but the extent of catch up in living standards is questioned – not least the existence of the **middle-income trap** when growing economies find it hard to sustain growth and rising per capita incomes beyond a certain level.

MICROFINANCE

- also called **microcredit**, is a type of banking service that is provided to unemployed or low-income individuals or groups who otherwise have no other access to financial services.
- While institutions participating in the area of microfinance are most often associated with lending (microloans can be anywhere from $100 to $25,000), many offer additional services, including bank accounts and micro-insurance products, and provide financial and business education.
- ***Ultimately, the goal of microfinance is to give impoverished people an opportunity to become self-sufficient.***

Microfinance services are provided to unemployed or low-income individuals because most of those trapped in poverty or with limited resources do not have enough income to do business with traditional financial institutions. Despite being excluded from banking services, however, those who live off of as little as $2 a day do attempt to save, borrow, acquire credit or insurance and make payments on their debts. As a result, many look for help from family, friends and even loan sharks, who often charge exorbitant interest rates.

Microfinance allows people to safely take on reasonable small business loans in a manner that is consistent with ethical lending practices. Although they exist all around the world, the majority of microfinancing operations occur in developing nations, such as Uganda, Indonesia, Serbia and Honduras. Many microfinance institutions (MFIs) focus on helping women in particular.

HOW MICROFINANCE WORKS

- Microfinancing organizations support a wide range of activities, ranging from business start-up capital to educational programs that allow people to develop the skills necessary to succeed as an entrepreneur. These programs can focus on such skills as bookkeeping, cash flow management and even technical or professional skills. Unlike typical financing situations, in which the lender is primarily concerned with the borrower having enough collateral to cover the loan, many microfinance organizations focus on helping entrepreneurs succeed.
- In many instances, people looking to join microfinance organizations are first required to take a basic money management class. Lessons focus on understanding interest rates and the concept of cash flow, how financing agreements and savings accounts work, how to budget, and how to manage debt.
- Once educated, customers are then allowed access to loans. Just as one would find at a traditional bank, a loan officer approves and helps borrowers with applications and oversight. The typical loan, sometimes as little as $100, does not seem like much to many in the developed world. But to many impoverished people, this figure is enough to start a business or engage in other profitable activities

MICROFINANCE LOAN TERMS

- Like conventional lenders, microfinanciers must charge interest on loans, and they institute specific repayment plans with payments due at regular intervals. Some require loan recipients to set aside parts of their income in a savings account used as insurance in case of default; if the borrower repays the loan successfully, he has use of this account, of course.
- Because many applicants cannot offer any collateral, microlenders often pool borrowers together, as a buffer. After receiving loans, recipients repay their debts together. Because the success of the program depends on everyone's contributions, a form of peer pressure helps ensure loan repayment. For example, if an individual is having trouble using his or her money to start a business, that person can seek help from other group members or from the loan officer. Through repayment, loan recipients start to develop a good credit history, allowing them to obtain larger loans down the line.
- Interestingly, even though the borrowers often qualify as very poor, repayment rates on microloans are often higher than the average rate on more conventional forms of financing. For example, the microfinancing institution Opportunity International reported repayment rates of approximately 98.9% in 2016.

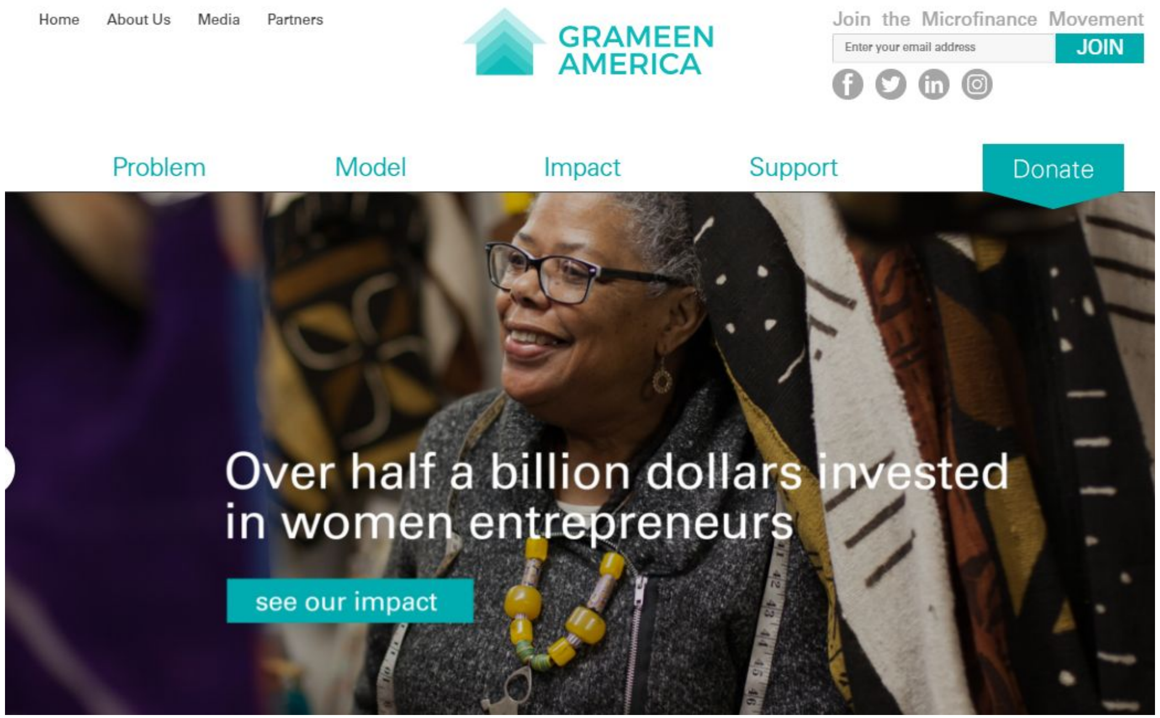
HISTORY OF MICROFINANCE

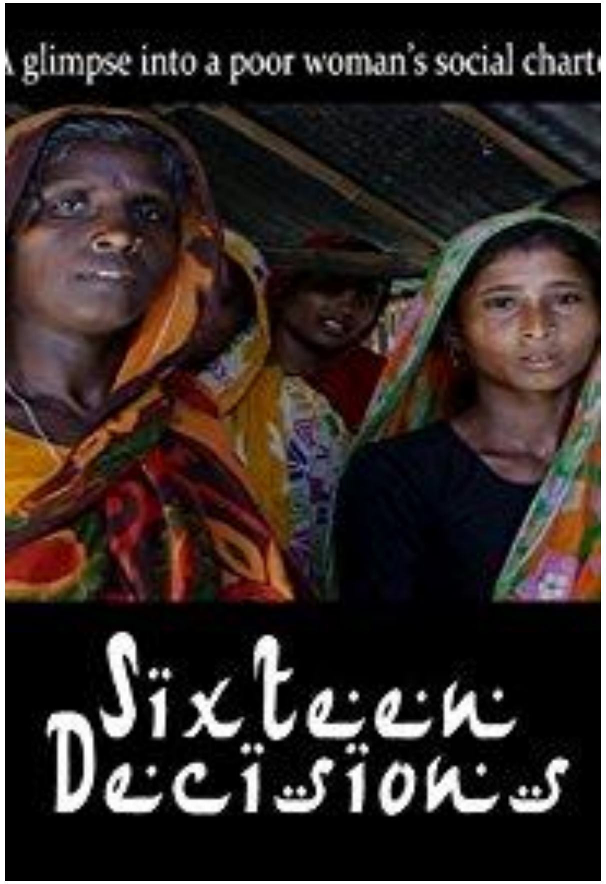
- Microfinance is not a new concept: Small operations have existed since the **18th century**. The first occurrence of microlending is attributed to the Irish Loan Fund system, introduced by Jonathan Swift, which sought to improve conditions for impoverished Irish citizens.
- But in its modern form, microfinancing became popular on a large scale in the **1970s**. The first organization to receive attention was **the Grameen Bank**, which was started in 1976 by Muhammad Yunus in Bangladesh. On top of providing loans to its clients, the Grameen Bank also suggests its customers subscribe to its "**16 Decisions**," a basic list of ways the poor can improve their lives. The "16 Decisions" touch on a wide variety of subjects ranging from a request to stop the practice of issuing dowries upon a couple's marriage to ensuring drinking water is kept sanitary*. In 2006, the Nobel Peace Prize was awarded to both Yunus and the Grameen Bank for their efforts in developing the microfinance system*.

http://www.grameen.com/16-decisions/

1.0 We shall follow and advance the four principles of Grameen Bank – Discipline, Unity, Courage and Hard work – in all walks of our lives.
2.0 Prosperity we shall bring to our families.
3.0 We shall not live in dilapidated houses. We shall repair our houses and work towards constructing new houses at the earliest.
4.0 We shall grow vegetables all the year round. We shall eat plenty of them and sell the surplus.
5.0 During the plantation seasons, we shall plant as many seedlings as possible.
6.0 We shall plan to keep our families small. We shall minimize our expenditures. We shall look after our health.
7.0 We shall educate our children and ensure that they can earn to pay for their education.
8.0 We shall always keep our children and the environment clean.
9.0 We shall build and use pit-latrines.
10.0 We shall drink water from tubewells. If it is not available, we shall boil water or use alum.
11.0 We shall not take any dowry at our sons' weddings, neither shall we give any dowry at our daughters wedding. We shall keep our centre free from the curse of dowry. We shall not practice child marriage.
12.0 We shall not inflict any injustice on anyone, neither shall we allow anyone to do so.
13.0 We shall collectively undertake bigger investments for higher incomes.
14.0 We shall always be ready to help each other. If anyone is in difficulty, we shall all help him or her.
15.0 If we come to know of any breach of discipline in any centre, we shall all go there and help restore discipline.
16.0 We shall take part in all social activities collectively.,

- documentary film
- directed and produced by Gayle Ferraro,
- exploring the impact of the Grameen Bank on impoverished women in Bangladesh. The bank provides micro loans of about $60 each to the poor
- loaning $2.3B to 10 million women



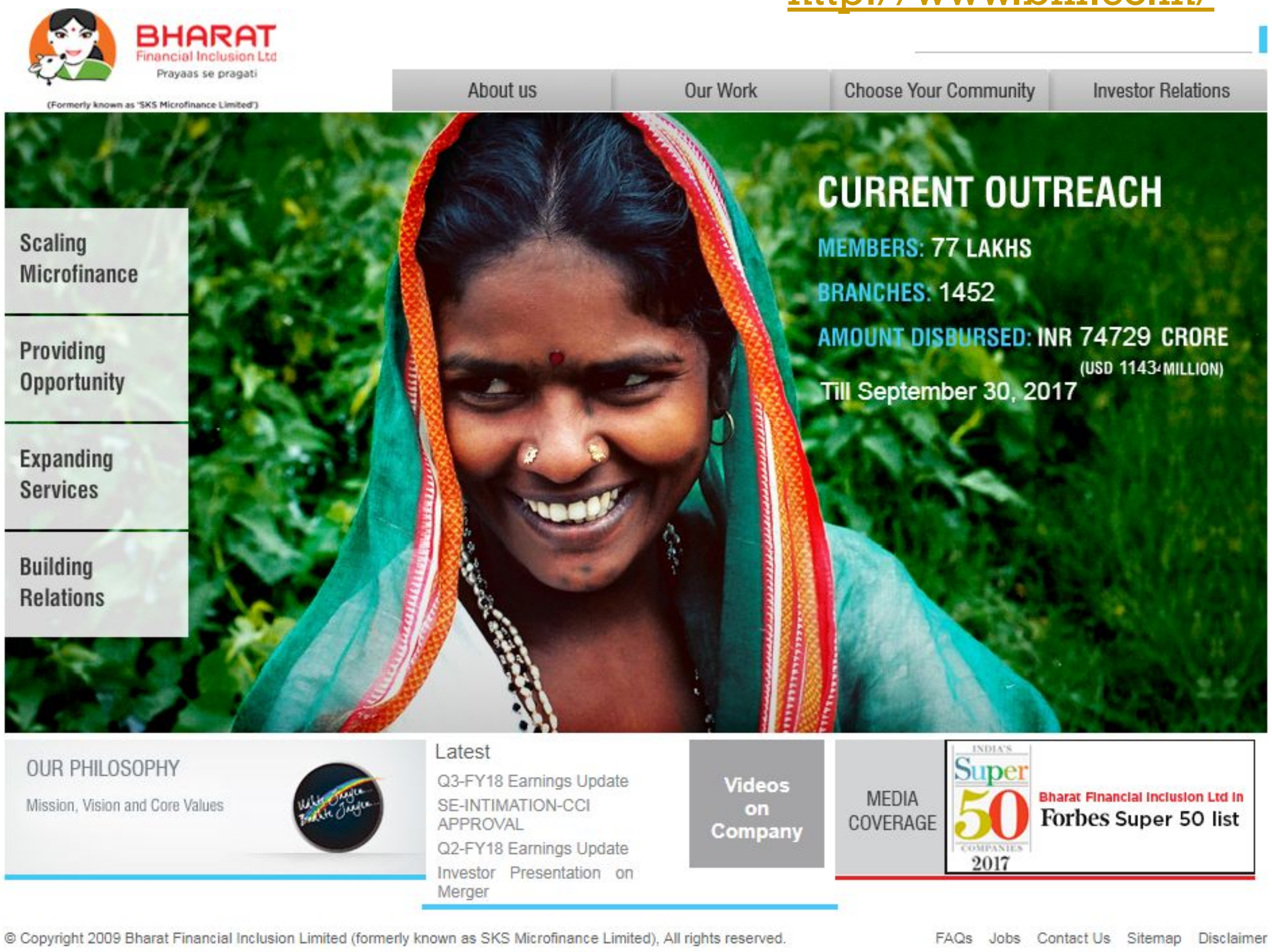


http://www.grameenamerica.com/
http://www.grameenamerica.org/2016annualreport/

HISTORY OF MICROFINANCE

- India's **SKS Microfinance** also serves a large number of poor clients. Formed in **1998**, it has grown to become one of the biggest microfinance operations in the world. SKS works in a similar fashion to the Grameen Bank, pooling all borrowers into groups of five members who work together to ensure loan repayment.
- There are other microfinance operations around the world. Some larger organizations work closely with the World Bank, while other smaller groups operate in different nations. Some organizations enable lenders to choose exactly who they want to support, categorizing borrowers on criteria like level of poverty, geographical region and type of small business. Others are very specifically targeted: There are those in Uganda, for example, that focus on providing women with capital required to undertake projects such as growing eggplants and opening small cafés. Some groups tend to focus their efforts only on businesses which are created with the intent of improving the overall community through initiatives like education, job training and clean water.

http://www.bfil.co.in/



SKS Microfinance renamed Bharat Financial Inclusion (June 13, 2016)

Earlier in May, the company had said the decision to change the name was taken as its core had undergone a transformation, equipping it to play a major role in fulfilling the national priority of financial inclusion.

The company is among the largest microfinance companies in India. It has presence across 18 states covering 1,00,000 villages, catering to its 63.65 lakh women members.

The company was mired in serious controversy in late 2010 due to rising spate of suicide ..

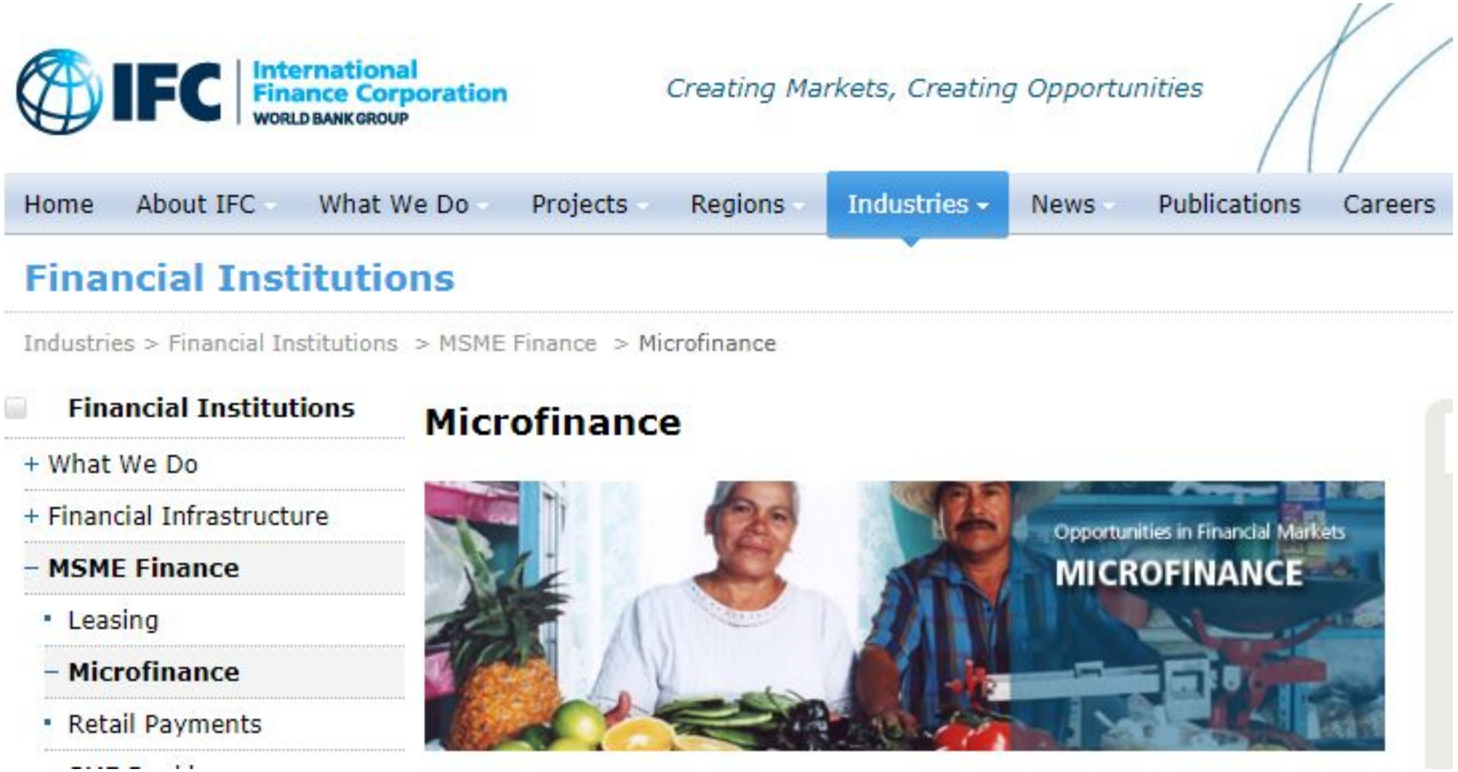
MICRO FINANCE FIRMS IN INDIA WITH BANKING LICENSE NEED TO BE CAREFUL AS TO NOT SERVICE THE RICH NOW: MUHAMMAD YUNUS

- Muhammed Yunus , founder and managing director of Grameen Bank said that the youth of today aided with technology should make the social impact that the previous generations could not. Yunus said that unemployment is no longer a worry of the developing nations as countries like large chunk of youth in Italy and Greece too are suffering from joblessness.
- ET asked him on the sidelines of One Young World what are the challenges faced in microfinance where one hand you have banking lice .. ET asked him on the sidelines of One Young World what are the challenges faced in microfinance where one hand you have banking licenses rolled out and on another, ponzy scams are preventing many from investing in them. Yunus said that often there are some who start micro-financing thinking of it as another business where they need to rake in the profits and then get greedy. He said the Reserve Bank of India granting licenses to some of the micro-finance institutes was a step in the right direction, but cautioned that those banks now need to be careful that they should stop lending the poor and go back serving the rich.

https://economictimes.indiatimes.com/industry/banking/finance/micro-finance-firms-in-india-with-banking-license-need-to-be-careful-as-to-not-service-the-rich-now-muhammad-yunus/articleshow/49846358.cms

BENEFITS OF MICROFINANCE

- The World Bank estimates that more than 500 million people have directly or indirectly benefited from microfinance-related operations. The **International Finance Corporation** (IFC), part of the larger World Bank Group, estimates that more than 130 million people have directly benefited from microfinance-related operations. However, these operations are only available to approximately 20% of the 3 billion people who qualify as part of the world's poor.
- In addition to providing microfinancing options, the IFC has assisted developing nations in the creation or improvement of **credit reporting bureaus** in 30 nations. It has also advocated for the addition of relevant laws governing financial activities in 33 countries.
- The benefits of microfinance extend beyond the direct effects of giving people a source for capital. Entrepreneurs who create a successful business create jobs, trade and overall economic improvement within the community. Empowering women in particular, as many MFIs do, leads to more stability and prosperity for families.



The evolution of the industry has been driven by many factors which include

- the transformation of microfinance providers,
- the sizable supply gap for basic financial services,
- the expansion of funding sources supporting the industry and the use of technology.

As the industry has developed, there has been a shift from specialized NGOs to an increasing number of regulated and licensed MFIs which stress that sustainability and impact go hand in hand. Furthermore, The World Bank Group is working with private microfinance institutions and stakeholders to incorporate responsible finance practices into all aspects of business operations. When done responsibly, private microfinance can have significant development impact and improve people’s lives.

THE FOR-PROFIT MICROFINANCE CONTROVERSY

- While there are countless heartwarming success stories ranging from micro-entrepreneurs starting their own water supply business in Tanzania to a $1,500 loan allowing a family to open a barbecue restaurant in China, to immigrants in the U.S. being able to build their own business, microfinance has sometimes falls under criticism.
- While microfinance **interest rates** are generally lower than conventional banks', critics have charged that these operations are making money off of the poor – especially since the trend in for-profit MFIs, such as BancoSol in Bolivia and the above-mentioned SKS (which actually began as a **nonprofit organization** (NPO), but became for-profit in 2003).
- One of the largest, and most controversial, is Mexico's Compartamos Banco. The bank was started in 1990 as a nonprofit. However, 10 years later, management decided to transform the enterprise into a traditional, for-profit company. In 2007, it went public on the Mexican Stock Exchange, and its **initial public offering** (IPO) raised more than $400 million. Like most other microfinance companies, Compartamos Banco makes relatively small loans, serves a largely female clientele, and pools borrowers into groups. The main difference comes with its use of the funds it nets in interest and repayments: Like any public company, it distributes them to shareholders. In contrast, nonprofit institutions take a more philanthropic bent with any profits, using them to expand the number of people it helps or create more programs.

THE FOR-PROFIT MICROFINANCE CONTROVERSY (2)

- In addition to Compartamos Banco, many major financial institutions and other large corporations have launched for-profit microfinance projects. CitiGroup (NYSE:C), Barclay's (NYSE:BCS) and General Electric (NYSE:GE) have started microfinance divisions in many countries, for example. Other companies have created mutual funds that invest primarily in microfinance firms.
- Compartamos Banco and its for-profit ilk have been criticized by many, including the grandfather of modern microfinance himself, Muhammad Yunus. The immediate, pragmatic fear is that, out of desire to make money, these MFIs will charge higher interest rates that may create a debt trap for low-income borrowers. But Yunus and others also have a more fundamental concern: that the incentive for microcredit should be poverty alleviation, not profit. By their very nature (and their obligation to stockholders), these publicly traded firms work against the original mission of microfinance – helping the poor above all else.
- In response, Compartamos and other for-profit MFIs counter that commercialization allows them to operate more efficiently, and to attract more capital by appealing to profit-seeking investors. By becoming a profitable business, their argument goes, an MFI is able to extend its reach, providing more money and more loans to low-income applicants.
- For now, charitable and commercialized MFIs co-exist.

THE MICROFINANCE DELUSION: WHO REALLY WINS?


The Economic Times | Finance

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04:05 PM | 05 MAR CLOSED MARKET STATS

Sponsored Mutual Funds DSP BlackRock Tax Saver Direct Plan-Growth NAV ₹47.15 Day Change -0.45 (-0.95%)

Microfinance: What's wrong with it


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The microfinance delusion: who really wins?

Jason Hickel

most popular

Live Crystal Palace 2-3 Manchester United: Premier League - as it happened


TIME

What Went Wrong with Microfinance?

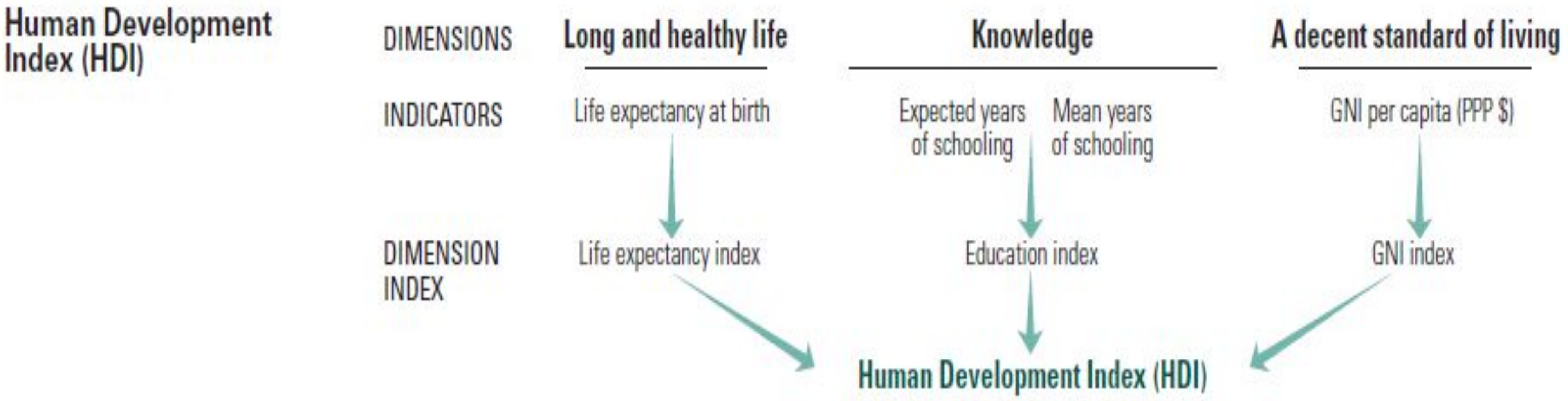
By Knowledge@Wharton | March 14, 2012

CRISES POINTS

- Banks
- Monetary Financial Institutions (**MFIs**)
- Credit Culture
- Labour Slowdown
- Politics

HDI

- The HDI was created to emphasize that people and their capabilities should be the ultimate criteria for assessing the development of a country, not economic growth alone. The HDI can also be used to question national policy choices, asking how two countries with the same level of GNI per capita can end up with different human development outcomes. These contrasts can stimulate debate about government policy priorities.
  The Human Development Index (HDI) is a summary measure of average achievement in key dimensions of human development: a long and healthy life, being knowledgeable and have a decent standard of living. The HDI is the geometric mean of normalized indices for each of the three dimensions.
- The HDI simplifies and captures only part of what human development entails. It does not reflect on inequalities, poverty, human security, empowerment, etc.



21st century skills

Ways of thinking	Tools for working	Ways of working	Skills for living in the world
Creativity Critical thinking Problemsolving Decisionmaking Learning	Information and communication technology Information literacy	Communication Collaboration	Citizenship Life and career Personal and social responsibility

- [HDI map]

		Human Development Index	Inequality-adjusted HDI			Gender Development Index		Gender Inequality Index		
		Value	Value	Overall loss (%)	Difference from HDI rank[b]	Value	Group[c]	Value	Rank	
HDI rank		2015	2015	2015	2015	2015	2015	2015	2015	Va
VERY HIGH HUMAN DEVELOPMENT										
1	Norway	0.949	0.898	5.4	0	0.993	1	0.053	6	
2	Australia	0.939	0.861	8.2	–1	0.978	1	0.120	24	
2	Switzerland	0.939	0.859	8.6	–4	0.974	2	0.040	1	
4	Germany	0.926	0.859	7.2	–1	0.964	2	0.066	9	
5	Denmark	0.925	0.858	7.2	–2	0.970	2	0.041	2	
5	Singapore	0.925	..	..	..	0.985	1	0.068	11	
7	Netherlands	0.924	0.861	6.9	2	0.946	3	0.044	3	
8	Ireland	0.923	0.850	7.9	–2	0.976	1	0.127	26	
9	Iceland	0.921	0.868	5.8	6	0.965	2	0.051	5	
10	Canada	0.920	0.839	8.9	–2	0.983	1	0.098	18	
10	United States	0.920	0.796	13.5	–10	0.993	1	0.203	43	
12	Hong Kong, China (SAR)	0.917	..	..	..	0.964	2	..	..	
13	New Zealand	0.915	..	..	..	0.963	2	0.158	34	
14	Sweden	0.913	0.851	6.7	3	0.997	1	0.048	4	
15	Liechtenstein	0.912	..	..	..	..	..	..	..	
16	United Kingdom	0.909	0.836	8.0	–1	0.964	2	0.131	28	
17	Japan	0.903	0.791	12.4	–8	0.970	2	0.116	21	
18	Korea (Republic of)	0.901	0.753	16.4	–19	0.929	3	0.067	10	
19	Israel	0.899	0.778	13.5	–11	0.973	2	0.103	20	
20	Luxembourg	0.898	0.827	8.0	1	0.966	2	0.075	13	
21	France	0.897	0.813	9.4	–1	0.988	1	0.102	19	

177	Liberia	0.427	0.284	33.4	1	0.830	5	0.649	150
178	Guinea-Bissau	0.424	0.257	39.3	–5	..	..	..	..
179	Eritrea	0.420	..	..	..	..	..	..	..
179	Sierra Leone	0.420	0.262	37.8	–3	0.871	5	0.650	151
181	Mozambique	0.418	0.280	33.0	3	0.879	5	0.574	139
181	South Sudan	0.418	..	..	..	..	..	..	..
183	Guinea	0.414	0.270	34.8	2	0.784	5	..	..
184	Burundi	0.404	0.276	31.5	4	0.919	4	0.474	108
185	Burkina Faso	0.402	0.267	33.6	2	0.874	5	0.615	146
186	Chad	0.396	0.238	39.9	–1	0.765	5	0.695	157
187	Niger	0.353	0.253	28.3	1	0.732	5	0.695	157
188	Central African Republic	0.352	0.199	43.5	0	0.776	5	0.648	149

WORLD ECONOMICS: MIDDLE-INCOME TRAP / CHINA

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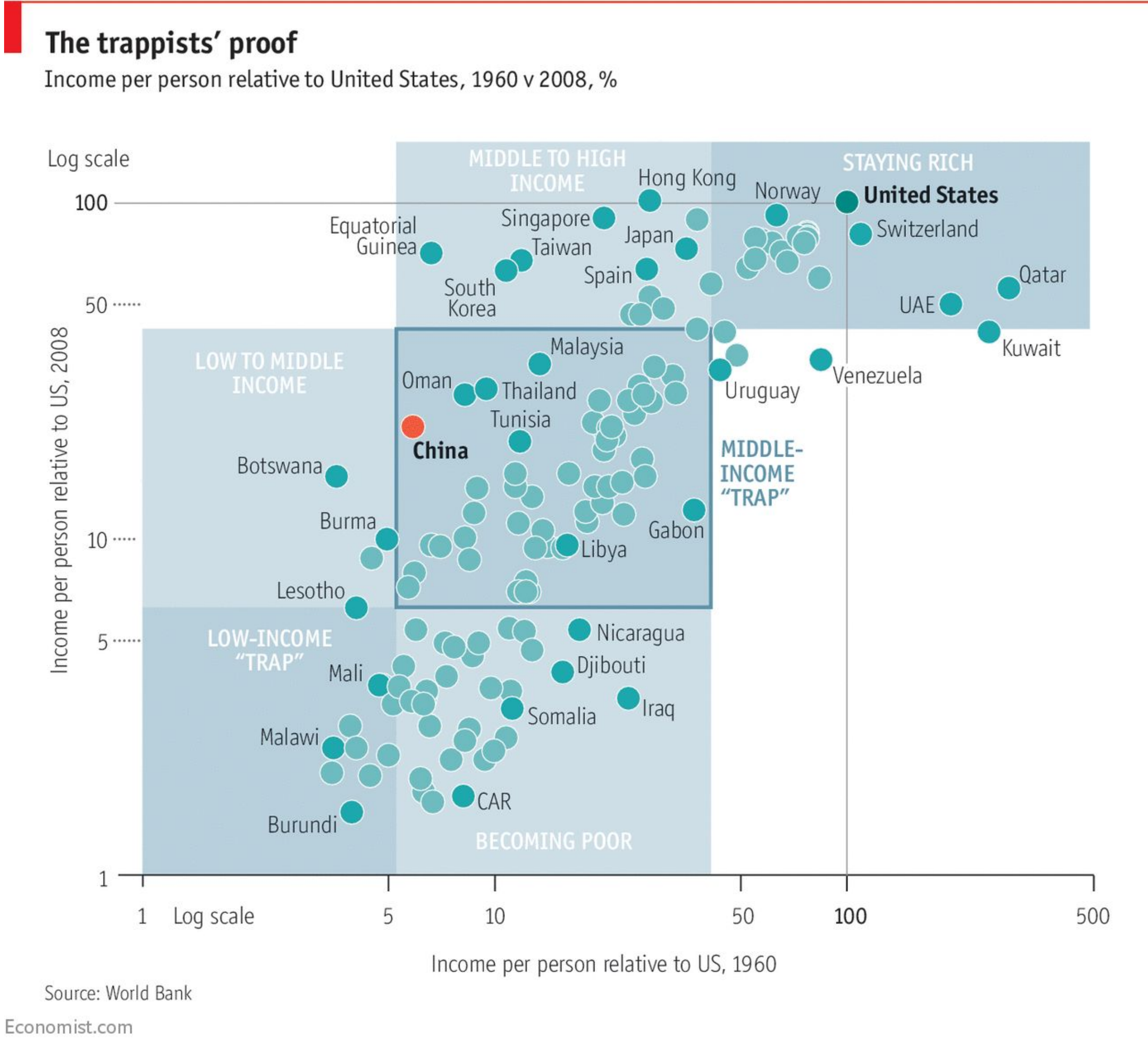
MIDDLE INCOME TRAP

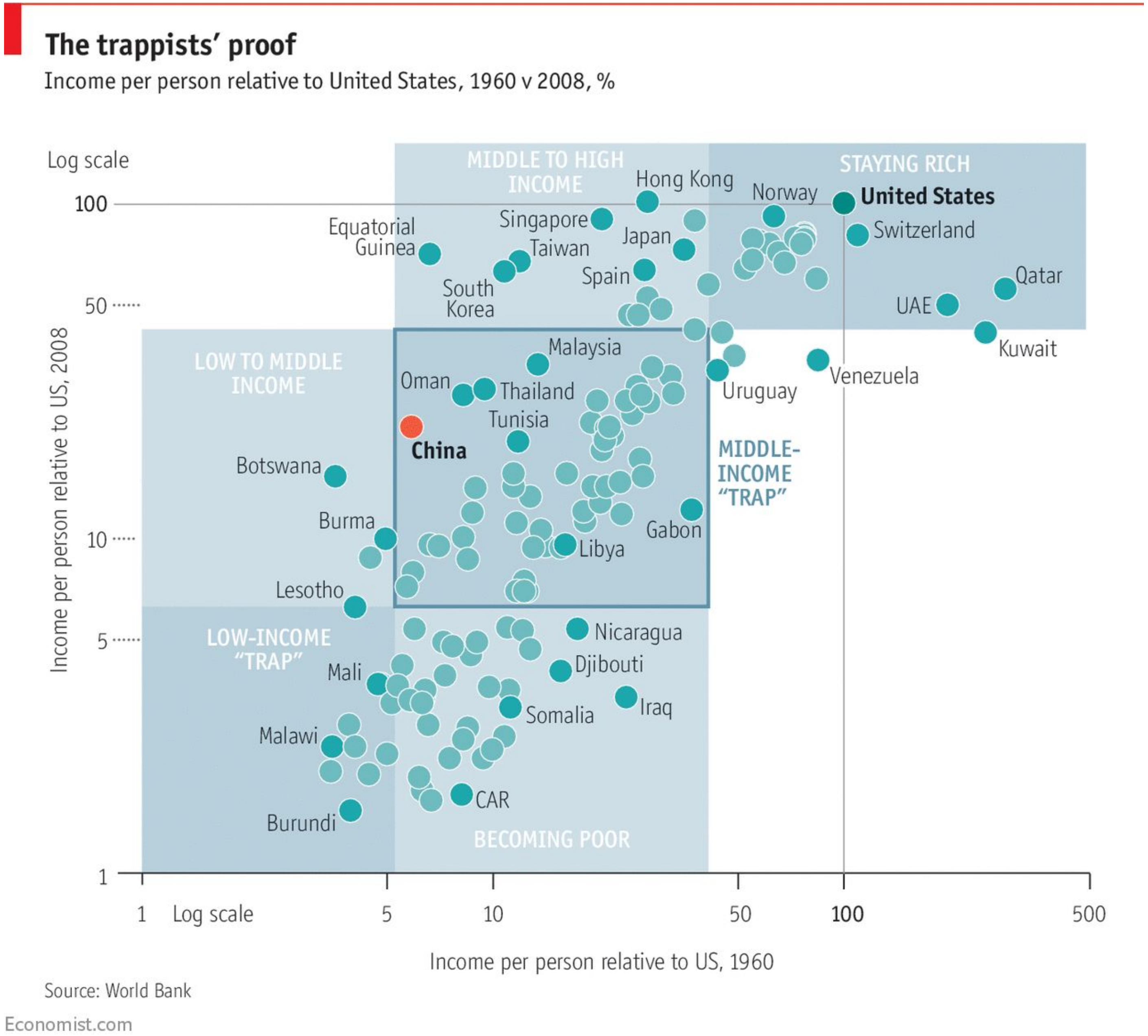
- Paul Krugman, "The Myth of Asia's Miracle", which re-examined the source of the tigers' success
- Geoffrey Garrett "Globalisation's Missing Middle" - *Middle-income countries have not done nearly as well under globalised markets as either richer or poorer countries.*
- Homi Kharas and Indermit Gill of the World Bank nvented the term "middle-income trap", which subsequently took on a life of its own
- The trap can be interpreted in a variety of ways, which may be one reason why so many people believe in it.
  - Some confuse the trap with the simple logic of catch-up growth. According to that logic, poorer countries can grow faster than richer ones because imitation is easier than innovation and because capital earns higher returns when it is scarce. By the same logic, a country's growth will naturally slow down as the gap with the leading economies narrows and the scope for catch-up growth diminishes. All else equal, then, middle-income countries should grow more slowly than poorer ones.
  - But (!) Mr Garrett was making a bolder argument: that middle-income countries tend to grow more slowly than both poorer and richer economies.

MIDDLE-INCOME TRAP

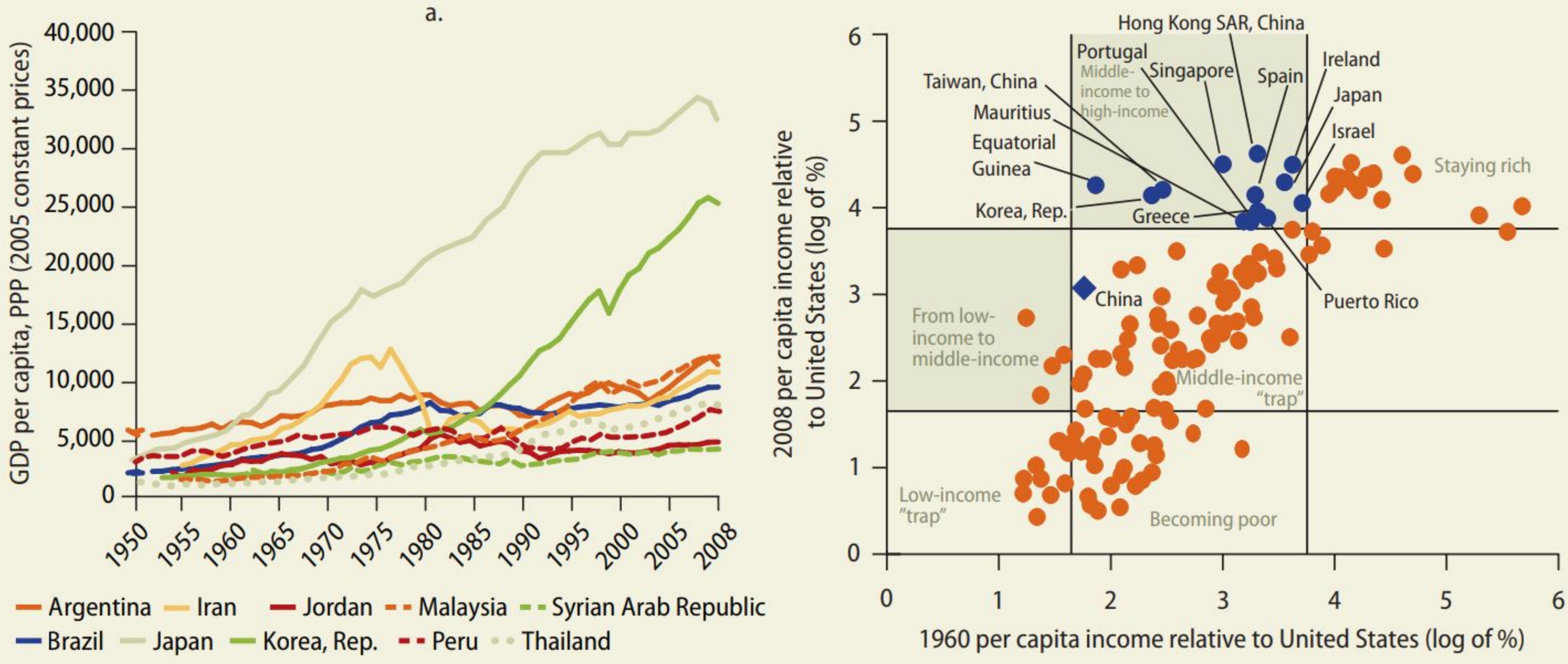
- By far the most prominent trap-watcher is **CHINA**, one of the few middle-income economies that is more than middle-sized.
  - In 2015 Lou Jiwei, then China's finance minister, said that his country had a 50% chance of falling into the trap in the next five to ten years.
  - The same fear haunts Liu He, an influential economic adviser to Xi Jinping, China's president. Mr Liu was one of the driving forces behind a report entitled "China 2030", published in 2012 by his Development Research Centre (DRC) and the World Bank. The report featured a chart that has perhaps done more than any other to spread the idea of a middle-income trap.
  - It showed that of 101 countries which counted as middle-income in 1960, only 13 had achieved high-income status by 2008. The rest spent the intervening 50 years trapped in mediocrity or worse.



- It defines "middle-income" broadly, including any country with a GDP per person that is more than 5.2% of America's (at purchasing-power parity) and less than 42.75%. That definition means that a country with a GDP per person of just $590 (at 1990 prices) counted as middle income in 1960. And at the other end of the middle-income scale, a country with a GDP per person as high as $13,300 in 2008 would also still belong to the same category. The second number is more than 2,000% higher than the first. No wonder so many countries remained stuck in between them.



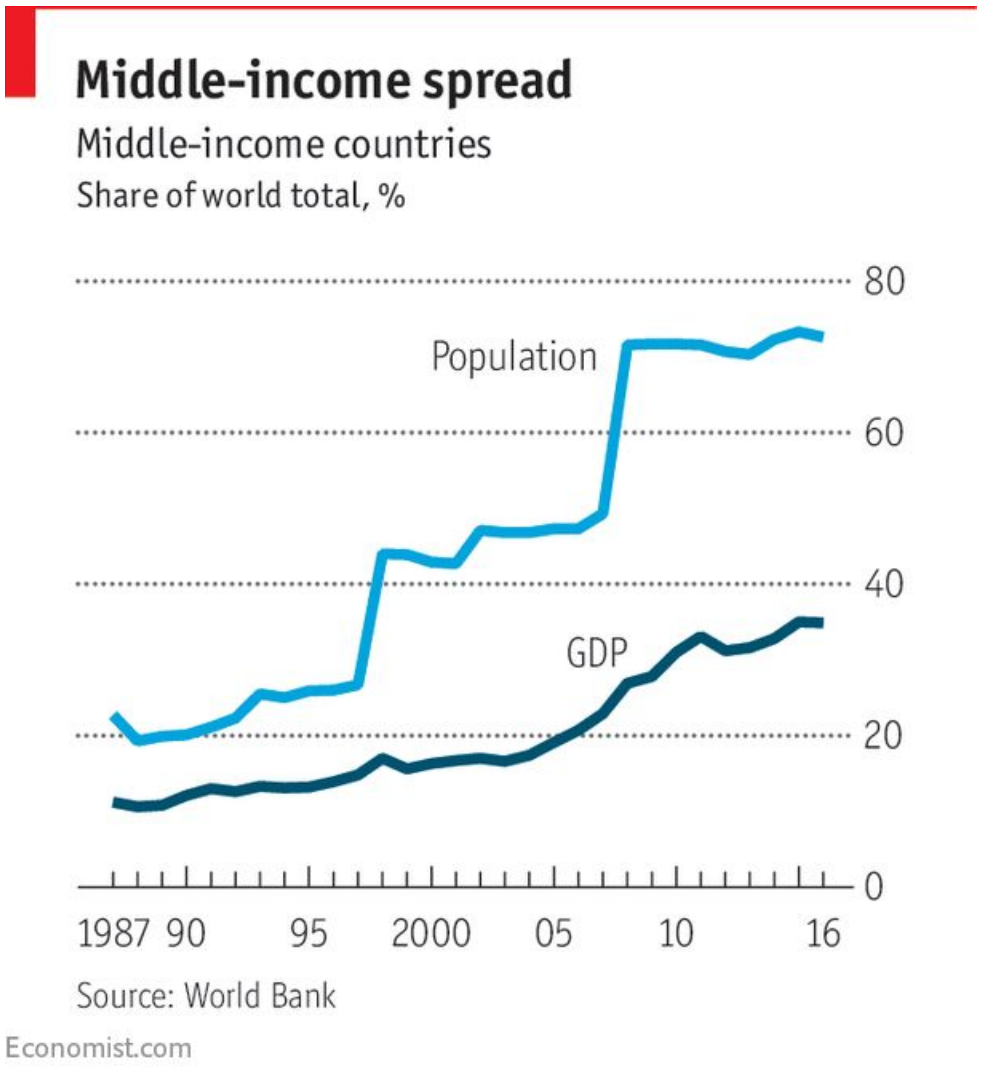
In principle, it would be possible for an economy's GDP per person to grow by over 6% a year for 48 years without escaping it. It is not that middle-income is unusually treacherous. It is just that the definition is unusually capacious.



a.
GDP per capita, PPP (2005 constant prices)
40,000
35,000
30,000
25,000
20,000
15,000
10,000
5,000
0
1950
1955
1960
1965
1970
1975
1980
1985
1990
1995
2000
2005
2008
Argentina
Iran
Jordan
Malaysia
Syrian Arab Republic
Brazil
Japan
Korea, Rep.
Peru
Thailand
Hong Kong SAR, China
Portugal
Middle-income to high-income
Singapore
Spain
Ireland
Japan
Israel
Taiwan, China
Mauritius
Equatorial Guinea
Korea, Rep.
Greece
Staying rich
China
Puerto Rico
From low-income to middle-income
Middle-income "trap"
Low-income "trap"
Becoming poor
2008 per capita income relative to United States (log of %)
1960 per capita income relative to United States (log of %)
0
1
2
3
4
5
6

COUNTRIES THAT ARE NEITHER RICH NOR POOR CAN HOLD THEIR OWN AGAINST RIVALS AT BOTH EXTREMES

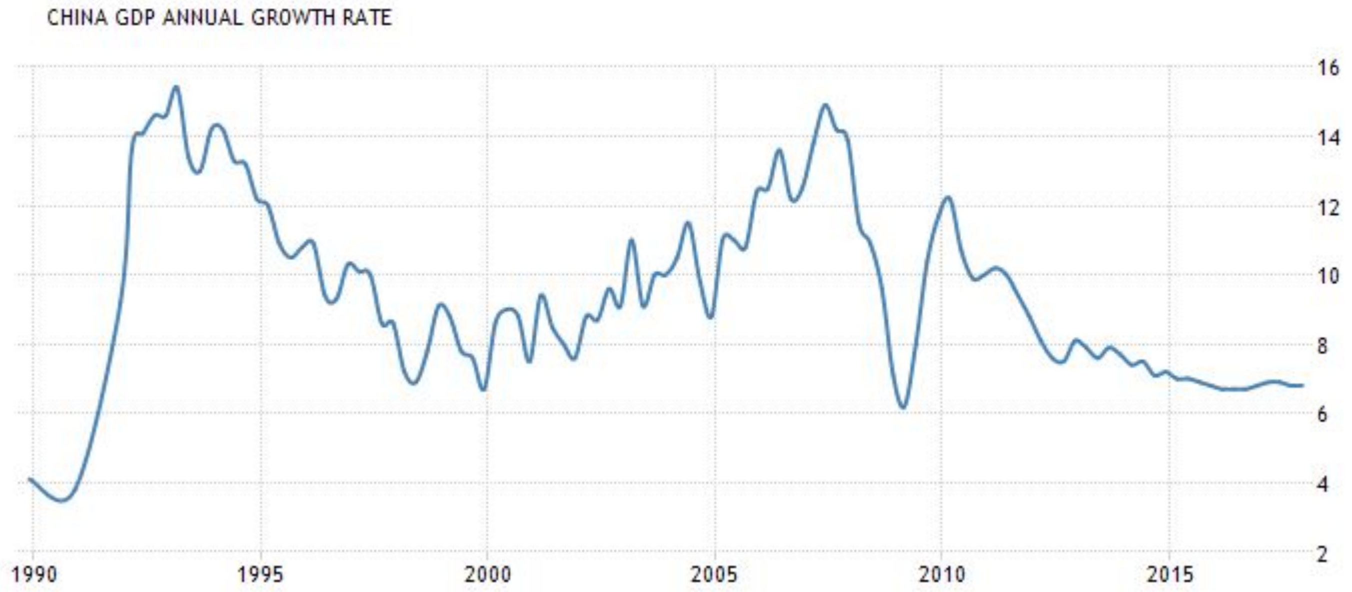
- Slow and queasy
  - it seems to make sense that middle-income countries will be squeezed between higher-tech and lower-wage rivals on either side. *But those rivals rely on high technology or low wages for a reason.*
    - Rich economies need advanced technologies and skills to offset high wages.
    - Poor countries, for their part, need low wages to offset low levels of technology and skill.
    - The obvious conclusion is that middle-income countries can and do compete with both, combining middling wages with middling levels of skill, technology and productivity.



MIDDLE-INCOME TRAP

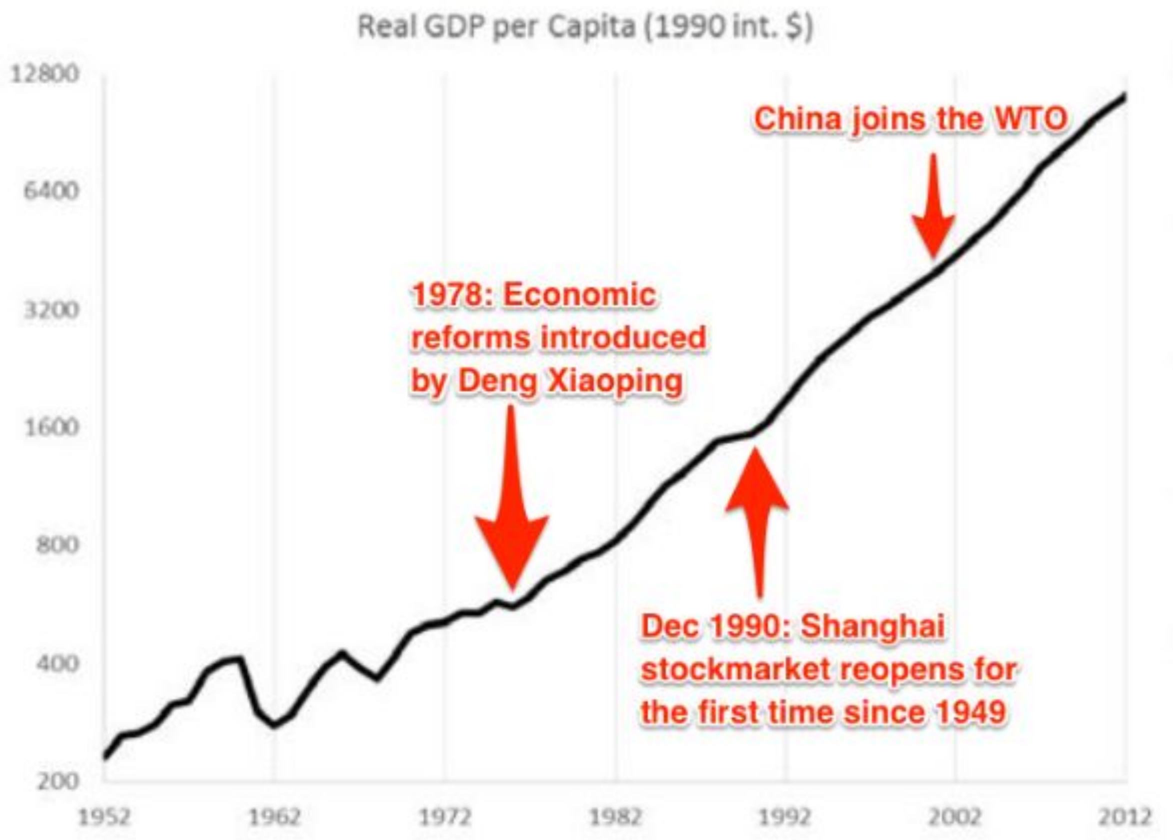
- Middle-income countries are often more accurately described as mixed-income economies.
- Shaping the mix are at least **four possible sources of growth in GDP per person**.
  1. moving workers from overmanned fields to more productive factories (structural transformation).
  2. adding more capital such as machinery per worker (capital-deepening).
  3. augmenting capital or labour by making it more sophisticated, perhaps by adopting techniques that a firm, industry or country has not previously embraced (technological diffusion).
  4. the final source of growth derives from advances in technology that introduce something new to the world at large (technological innovation).
- So development does not proceed in discrete stages that require a nationwide leap from one stage to the next. It is more like a long-distance race, with a leading pack and many stragglers, in which the result is an average of everyone’s finishing times. The more stragglers in the race, the more room for improvement.

CHINA GDP ANNUAL GROWTH RATE



HISTORY

- epresented the success of the First Five-Year Plan, during which "6000 Soviet advisers helped establish and operate the 156 large-scale capital intensive Soviet-assisted projects", significantly increasing the pace and quality (productivity) of industrialization in the country. However, it was followed by the Great Leap Forward (1958-1962), which undid many of the gains through worsening of incentives by banning material incentives and restricting markets.



HISTORY

- These reforms were then unwound between 1962 and 1966, leading to another period of productivity and per capita GDP growth, before the events of the Cultural Revolution (where strikers clashed with the authorities) set the economy back once again.
- the Third Plenary Session of the 11th Central Committee of the Communist Party in December 1978 was the defining moment in shifting the country from its unsteady early economic trajectory on to a more sustainable path. It laid the groundwork for future growth by introducing reforms that allowed farmers to sell their produce in local markets and began the shift from collective farming to the household responsibility system.
- A year later the Law on Chinese Foreign Equity Joint Ventures was introduced, allowing foreign capital to enter China helping to boost regional economies although it took until the mid-1980s for the government to gradually ease pricing restrictions and allow companies to retain profits and set up their own wage structures. This not only helped to boost GDP from an annual average of 6% between 1953-1978 to 9.4% between 1978-2012 but also increased the pace of urbanization as workers were drawn from the countryside into higher-paying jobs in cities.
- This process of market liberalization led to the establishment of China as a major global exporter. It eventually allowed for the reopening of the Shanghai stock exchange in December 1990 for the first time in over 40 years and, ultimately, to China's accession to the World Trade Organisation
- These reforms had a significant impact both on per capita GDP and the pace of the falling share of the labour force working in agriculture.

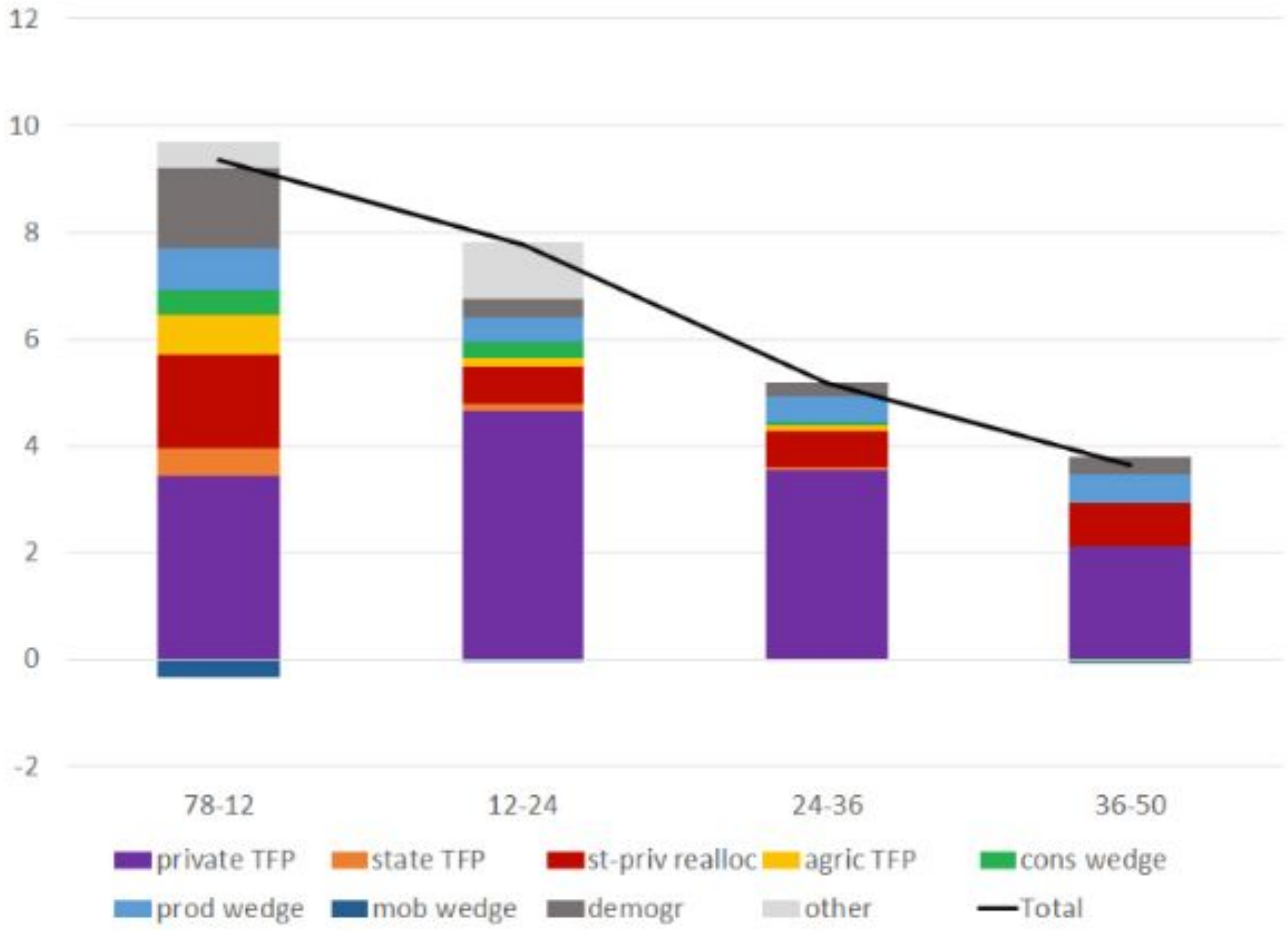


Figure 12: Actual and post-78 trend GDP growth.

HOW CHINA INTERFERES IN AUSTRALIA

- Few countries on the planet have benefited as clearly from China as Australia has. Its society has been enriched by waves of Chinese migrants and sojourners for 160 years. Its national income grew as much as 13 percent in a single decade as a result of China's resource-intensive construction boom, according to the Australian Reserve Bank. And an easing of the resources boom has been offset by the spending power of 180,000 Chinese students and a million tourists each year, along with hundreds of thousands of migrants who have mostly thrived in their new country.

ARE CHINA AND BRAZIL TRANSFORMING AFRICAN AGRICULTURE?

- Chinese and Brazilian engagements in four African countries – Ethiopia, Ghana, Mozambique and Zimbabwe – as well as the origins of Chinese and Brazilian agricultural policies, technology and capital by looking at the two countries' domestic contexts.
  - They reveal a rich mix of engagements, including:
  - agricultural investments by private and state owned enterprises
  - tri-lateral development cooperation efforts
  - technological adaptation initiatives
  - training programmes
  - 'under-the-radar' involvement in agriculture by Chinese migrants.
- These diverse experiences challenge simplistic narratives of either "South–South" collaboration or "neo-imperial" expansion of "rising powers".