

EE 460: Thai Economy

Rethinking growth strategies

The Middle Income Trap

Why Nations Fail by Acemoglu and Robinson

Thailand's *National Economic and Social Development Plans*

Sources of Happiness

Fragile states

Bhanupong

Lecture 2

Main Themes

The Middle Income Trap (MIT)

Rethinking growth strategies

Why Nations Fail

National Economic and Social Development Plans

Sources of Happiness

Fragile state Index

Middle vs. Upper Income Countries

From \$10,000 to \$20,000

- Robert Barro looked at countries that had at least doubled real per capita GDP since 1990. Within this group, he defined a middle-income success as having achieved a level of real per capita GDP in 2014 of at least \$10,000.
- An upper-income success requires a level of at least \$20,000 (the numbers are in 2011 US dollars and factor in international adjustments for changes in purchasing power).

Countries which doubled real per capita GDP since 1990:

- The world's **middle-income** convergence success stories comprise China, Costa Rica, Indonesia, Peru, Thailand, and Uruguay (Uruguay is a surprise, apparently boosted by dramatic migration of human capital out of Argentina.)
- The **upper-income** successes consist of Chile, Hong Kong, Ireland, Malaysia, Poland, Singapore, South Korea, and Taiwan.

Middle-Income Trap

- A view that has gained recent popularity is the ‘middle-income trap’. The successful transition from low- to middle-income status is typically followed by **barriers** that impede a further transition to upper income.
- ***The data suggest that this trap is a myth.***
- Moving from low- to middle-income status, as achieved recently by China, is difficult. Conditional on achieving middle-income status, the further transition to upper-income status is also difficult.
- However, there is no evidence that this second transition is harder than the first one (Robert Barro).
- ***If Barro is correct, how come Thailand has still stuck in the trap?***

GDP per capita can be raised over the long term by means of:

1. Capital deepening: an increase in the economy's stock of capital—plant and equipment—relative to its workforce.

2. Technological progress: the ability to produce more output without using any more inputs—capital or labor.

This is about raising productivity

(See Rodrick's economics of growth on one page)

Rethinking growth strategy: new development theories

- Growth is a complex process of economic, social, and political transformation.
- New economic concepts were created to capture some of its dimensions.
- Development *strategies follow* those new concepts in economic ***development theories***.

Early Development Theories

- Lewis: Dual economy, surplus labor

Economic Development with Unlimited Supplies of Labor.”
Manchester School 22 (May): 139–191

W. Arthur Lewis, a British citizen, was awarded the Nobel Prize in 1979 along with **Theodore Schultz** for “pioneering research into economic development ... with particular consideration of the problems of developing countries.

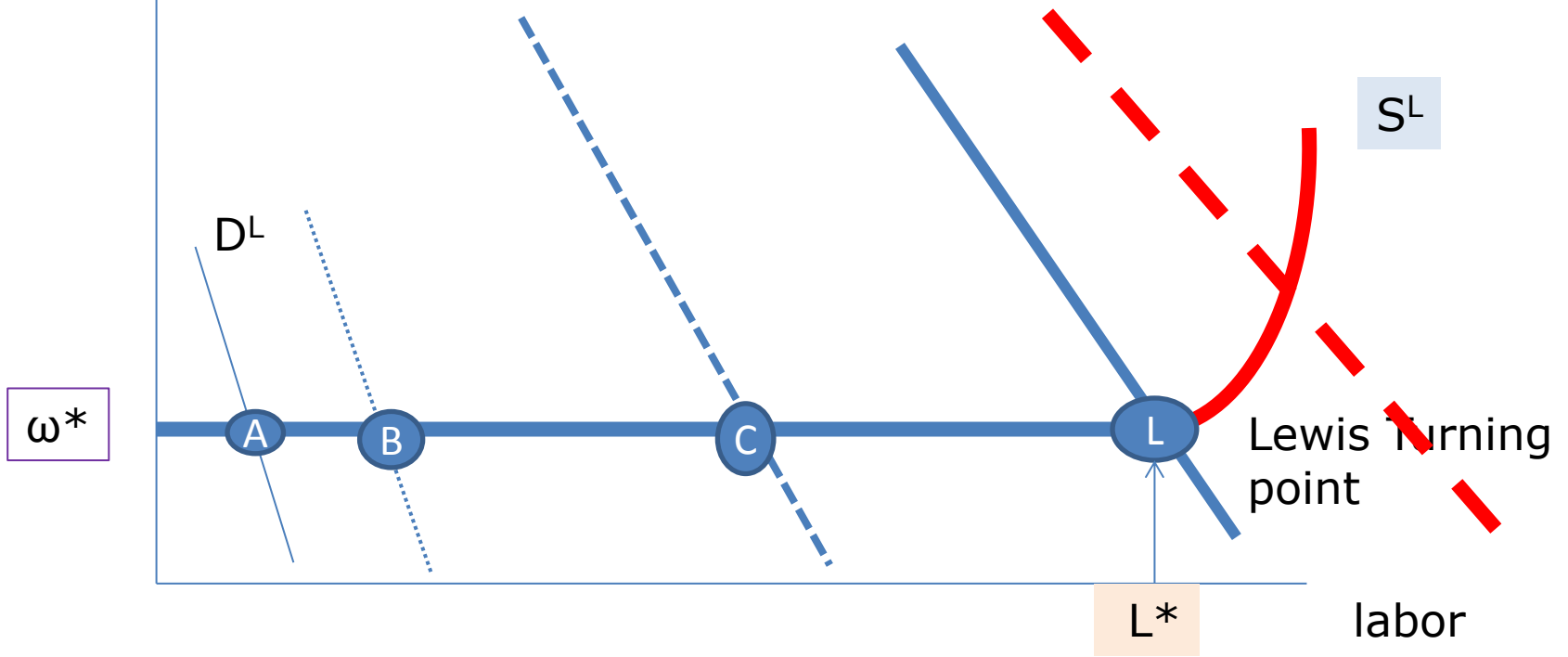
Lewis's Dual economy

- A poor country's economy can be thought of as containing two sectors, a small "capitalist" sector and a very large "traditional" (agricultural) sector.
- Employers in the capitalist sector hire people to make money. Employers in the traditional sector, on the other hand, are not profit maximizing and, therefore, hire too many people so that their productivity is very low.

Transforming agriculture to manufacturing

Wage

Expansion of demand for labor due to the rise of industrial output
Industrial profit rises as real wage rate remains constant
Until employment surpassing the L^*



Lewis's Strategy: Shift labor from agriculture to manufacturing

- Lewis argued on this basis that the way ***to spur development*** in poor countries is to shift labor into manufacturing, where it is more productive.
- The capitalists save out of their profit and use this saving to expand, which then adds to growth.
- *Has China (Cambodia) reached the Lewis turning point?*

Rostow, W.W. *The Stages of Economic Growth*.
Cambridge: Cambridge University Press, 1971

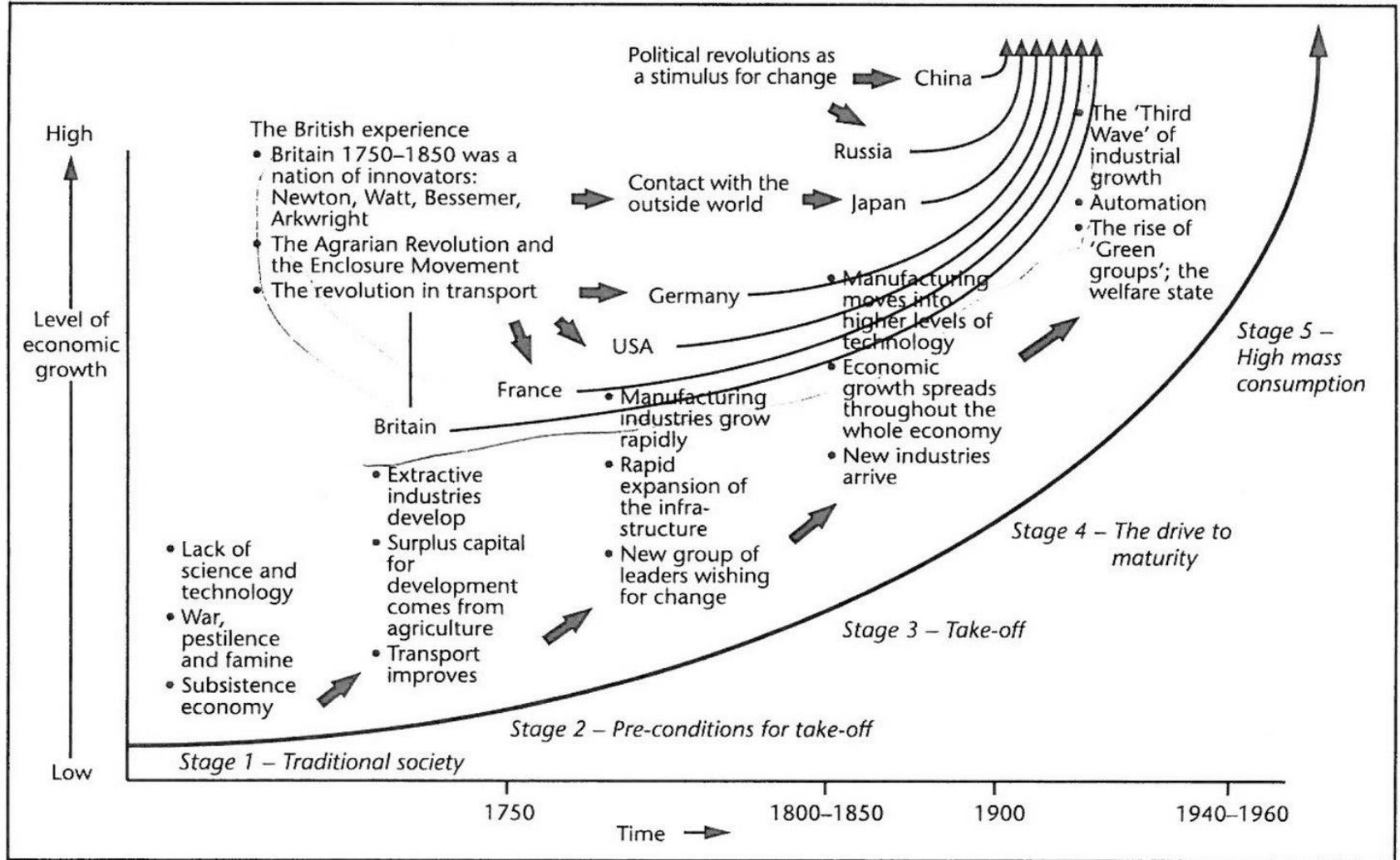
Five stages of economic growth

1. Traditional society (lack of science, subsistence economy)
2. Preconditions for take-off (surplus from agriculture, extractive industries and transportation develop)
3. Take-off (rise of manufacturing, rapid infrastructure development, new leaders wishing for changes)
4. The drive to maturity (new technology and new industries, growth spread through out the country)
5. High Mass Consumption (Third wave of industrial revolution, automation, and welfare state)

Rostow, W.W. *The Stages of Economic Growth*.

Cambridge: Cambridge University Press, 1971

Fig. 15.3: Rostow's model of economic growth as applied to selected countries.



Gershenkron, Alexander.

Economic Backwardness in Historical Perspective.

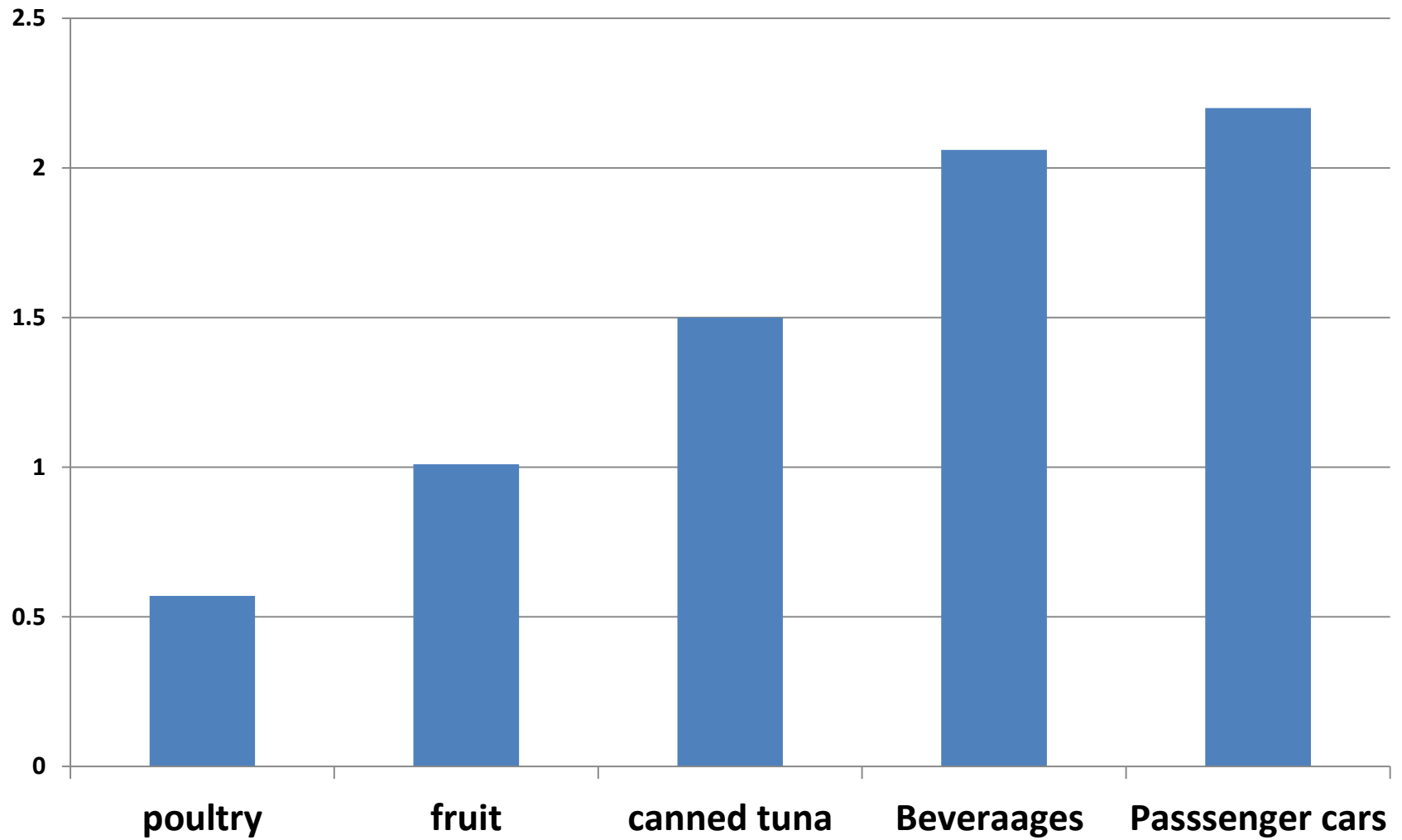
Cambridge: Harvard University Press, 1976

- Gershenkron differs from Rostow.
- The economic growth does not proceed as the stage of development theory suggested.
- The ***economic backwardness*** plays an important role of the progress of one economy and that would decide whether such economy will evolve into other stages or not.
- Is there any sign of economic backwardness in Thailand? Are we ready for Thailand 4.0 model of development?

The Singer-Prebisch thesis

- It focuses on terms of trade between primary products (raw materials and resources used in the productive process - metals, agricultural products) and manufactured goods.
- By examining data over a long period of time, Prebisch suggested that the terms of trade for primary commodities did have a tendency to decline since the income elasticity of demand for manufactured goods is greater than that for primary goods, especially food.

World income elasticity of Thailand's exports (1995-2015)



The Singer-Prebisch thesis

- As income increases, the demand for manufactured goods increases more rapidly relative to demand for primary products.
- As many developing countries tend to export primary products and import manufactured products, this implies the need to increase the volume of exports in order to keep importing the same level of manufactured and capital goods, or otherwise experience a deterioration of the trade balance.

The Singer-Prebisch thesis

- Due to the declining terms of trade primary products face, they concluded that developing countries should strive to diversify their economies and lessen dependence on primary commodities export through ***developing their own manufacturing*** industry by structural change and industrialization.
- Then came the idea of *inward-looking strategy*.

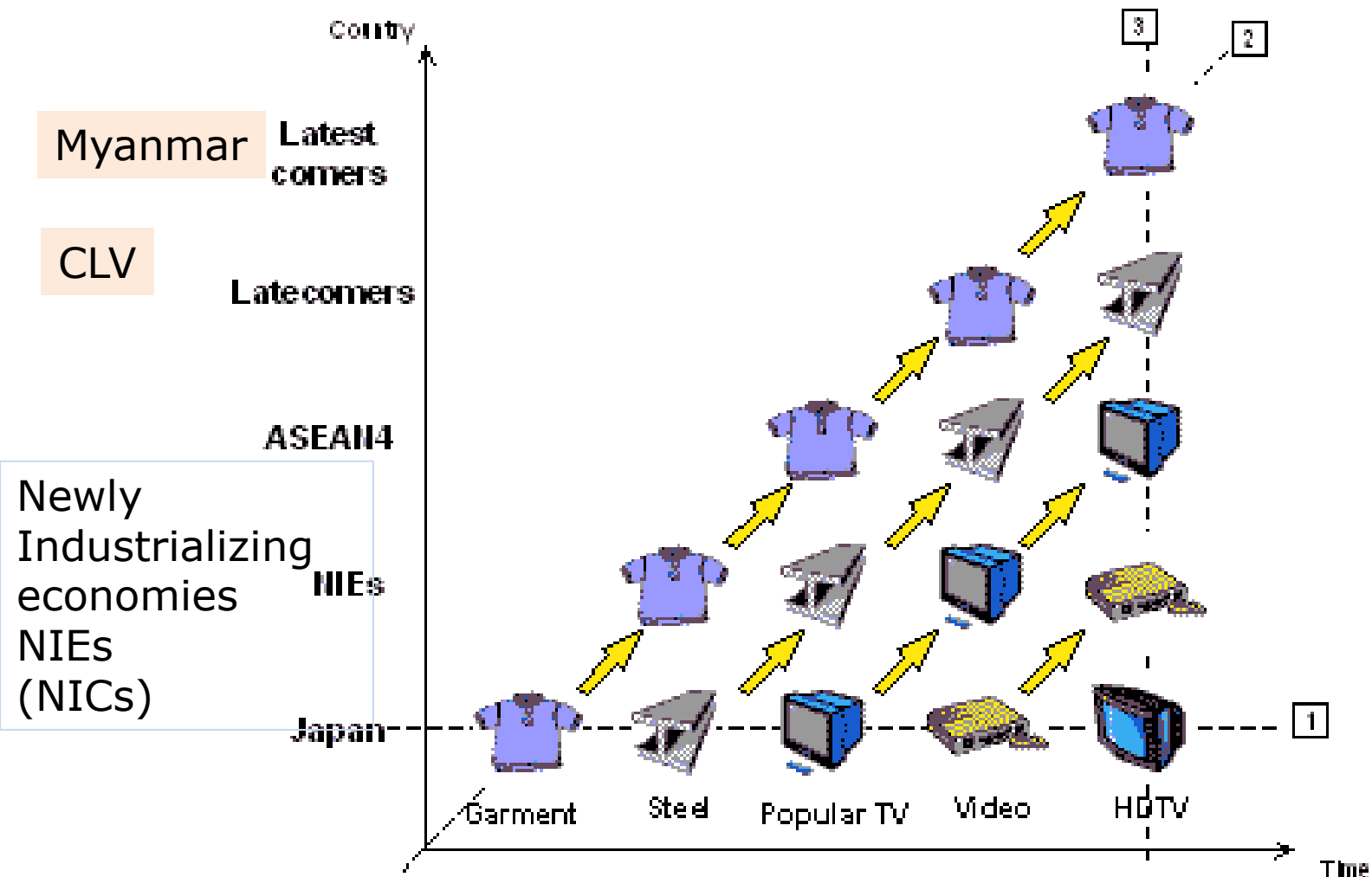
Akamatsu's flying geese

- Akamatsu's flying geese paradigm is a model for international division of labor in East Asia based on ***dynamic comparative advantage***.
- The paradigm postulated that Asian nations will catch up with the West as a part of a regional hierarchy where the production of commoditized goods would ***continuously move from the more advanced countries to the less advanced ones***.

Flying geese paradigm

- “The underdeveloped nations aligned successively behind the advanced industrial nations in the order of their different stages of growth in a wild-geese-flying pattern.
- "Depicting the catching-up process of post-war industrialization in Japan—a model successfully emulated by the East Asian ‘miracle’ economies, bringing hope to many other developing countries in Asia.

Structural Transformation in East Asia



Kaname Akamatsu (1935)

The metaphor of flying wild geese

- Sequential *shifting of comparative advantage* across economies, aided by factors such as foreign direct investment (**FDI**), structural change, infrastructure development, human capital formation, and industrial policy, unleashed trade-fueled economic development.

The FDI-driven economy

- *“FDI-driven economy” is the phrase used by many economists, meaning that foreign direct investment (FDI) is the major motive power for the national economy.*

How many years would it take to double GDP?

The rule of 72

- If an economy grows at x percent per year, output will double in $72/x$ years.
- If Thailand has a 9 percent annual growth rate, then real GDP will take 8 years to double $(72/9) = 8$.
- If would take 18 years to double GDP if it grows at 4 % annually, 24 years if 3%.
- Thailand's NESDB set 5% GDP growth target for 2017-21
- Too pessimistic (optimistic)?



There's No Such Thing as an Economic Miracle

Most of the world's wealthiest and best-governed countries got there without super-rapid bursts of growth.

Denmark, which has a per capita income of \$ 52,000 and is frequently ranked as one of the happiest countries in the world, never experienced what anyone would call an economic miracle.

The ability to maintain steady growth

- Denmark's overall economic record is gloriously boring.
- From 1890 to 1916, per capita growth averaged about 1.9 percent per year, and if in 1916 you had forecast that this pace would continue for another 100 years.
- Denmark had positive growth about 84 percent of the time and **no deep recessions**

Successful growers avoided downturns and kept growth *steady*

Number of years(1960-2002) which growth rate was:

	negative	<1	<2	>2
LDCs	14	19	24	18
Thailand	5	8	16	27
OECD	3	3	4	38

A Model of Asian Tigers

- Slow growth doesn't mean that the U.S. or Denmark were failures in the 19th century.
- It's hard for economies at or near the technological frontier to rapidly improve living standards, because invention is usually slower than playing catch-up by borrowing technologies from wealthier nations.
- Such borrowing of know-how, along with exports and rapid investments in education and infrastructure, is what later allowed the Asian tigers of Japan, South Korea, Taiwan, Hong Kong, Singapore and China to achieve growth rates of 8 percent to 10 percent a year.

Timeline of Thailand's development planning

1st Development Plan (1961-1966)

Import substitution

Infrastructure Investment

Promotion of private investment

Institutional establishment: Board of Investment (BOI) National Economic and Social Development Board (NESDB), Bureau of the budget (BOB), Fiscal Policy Office (FPO)

Early economic plans: Objectives and Missions

2nd Development plan (1967-1971)

Export promotion

Growth was driven by public investment in infrastructure

3rd Economic and social development plan (1972-1976)

Investment in rural area and education

Economic and Social Development Plans

4th Plan (1977-1981)

Increasing security spending,
Reducing social gaps,
Restoring *natural resources*

5th plan (1982-1986)

Public and private **cooperation**,
Rural development and investment

6th plan (1987-1991)

Maintain economic growth

Upgrade quality of life

7th plan (1992-1996)

income distribution,

improve quality of live and **environment**

Trend of (indicative) economic plans

8th plan (1997-2001)

Human-centered development

Public **participation**

Sustainable development

9th plan (2002-2006)

Competitiveness

Financial immune system

Self-reliant and resilient society

A policy shift in the 10th plan (2007-2011)

Sufficiency economy

Green growth

Sustainable development

The 11th National Economic and Social Development Plan (2012-2016)

- To develop Thailand into a **happy society** with equity, fairness, and resilience.
- Apart from promoting a peaceful society with good governance, the 11th Plan also aims to promote sustainable development through the restructuring of the economy, society, and politics, while nurturing natural resources and the environment.
- Another objective is to prepare the people and the community to be resilient to changes.

Richard Layard

Happiness

New York: Penguin Press, 2005

- Once subsistence income is guaranteed, making people happier is **not easy**.
- If we want people to be happier, we really have to know what conditions generate happiness and how to cultivate them.

Sources of happiness

1. Proportion of people who say that other people can be **trusted**.
2. Proportion of people who belong to **social organizations**.
3. Divorce rate
4. Unemployment rate
5. Religious belief
6. **Quality of government**

What makes people happy

- We are programmed to seek happiness.
- Humans are **social** beings, wanting to trust each other.
- People are deeply attached to the **status quo**.
- Human beings are **status conscious**.
- Human beings are very **adaptable**.
- **Extra income** increases happiness *less and less* as people get richer.

Fragile States

- The Fragile States Index, produced by The Fund for Peace, is a critical tool in highlighting not only the normal pressures that all states experience, but also in identifying when those ***pressures are pushing a state towards the brink of failure.***
- By highlighting pertinent issues in weak and failing states, The Fragile States Index makes political risk assessment and early warning of conflict accessible to policy-makers and the public at large.
- The Fragile States Index is an annual ranking of 178 nations based on their levels of stability and the pressures they face.

Social Indicators



Demographic Pressures

DP

Pressures on the population such as disease and natural disasters make it difficult for the government to protect its citizens or demonstrate a lack of capacity or will.

Includes pressures and measures related to:

- Natural Disasters
- Disease
- Environment
- Pollution
- Food Scarcity
- Malnutrition
- Water Scarcity
- Population Growth
- Youth Bulge
- Mortality



Refugees and IDPs

REF

Pressures associated with population displacement. This strains public services and has the potential to pose a security threat.

Includes pressures and measures related to:

- Displacement
- Refugee Camps
- IDP Camps
- Disease related to Displacement
- Refugees per capita
- IDPs per capita
- Absorption capacity



Group Grievance

GG

When tension and violence exists between groups, the state's ability to provide security is undermined and fear and further violence may ensue.

Includes pressures and measures related to:

- Discrimination
- Powerlessness
- Ethnic Violence
- Communal Violence
- Sectarian Violence
- Religious Violence



Human Flight and Brain Drain

HF

When there is little opportunity, people migrate, leaving a vacuum of human capital. Those with resources also often leave before, or just as, conflict erupts.

Includes pressures and measures related to:

- Migration per capita
- Human Capital
- Emigration of Educated Population

Economic Indicators



Uneven Economic Development

UED

When there are ethnic, religious, or regional disparities, the governed tend to be uneven in their commitment to the social contract.

Includes pressures and measures related to:

- GINI Coefficient
- Income Share of Highest 10%
- Income Share of Lowest 10%
- Urban-Rural Service Distribution
- Access to Improved Services
- Slum Population



Poverty and Economic Decline

ECO

Poverty and economic decline strain the ability of the state to provide for its citizens if they cannot provide for themselves and can create friction between the "haves" and the "have nots".

Includes pressures and measures related to:

- Economic Deficit
- Government Debt
- Unemployment
- Youth Employment
- Purchasing Power
- GDP per capita
- GDP Growth
- Inflation

Political and Military Indicators



State Legitimacy

SL

Corruption and a lack of representativeness in the government directly undermine the social contract.

Includes pressures and measures related to:

- Corruption
- Government Effectiveness
- Political Participation
- Electoral Process
- Level of Democracy
- Illicit Economy
- Drug Trade
- Protests and Demonstrations
- Power Struggles



Public Services

PS

The provision of health, education, and sanitation services, among others, are key roles of the state.

Includes pressures and measures related to:

- Policing
- Criminality
- Education Provision
- Literacy
- Water & Sanitation
- Infrastructure
- Quality Healthcare
- Telephony
- Internet Access
- Energy Reliability
- Roads

Political and Military Indicators



Human Rights and Rule of Law

HR

When human rights are violated or unevenly protected, the state is failing in its ultimate responsibility.

Includes pressures and measures related to:

- Press Freedom
- Civil Liberties
- Political Freedoms
- Human Trafficking
- Political Prisoners
- Incarceration
- Religious Persecution
- Torture
- Executions



Security Apparatus

SEC

The security apparatus should have a monopoly on the use of legitimate force. The social contract is weakened where this is affected by competing groups. *Includes pressures and measures related to:*

- Internal Conflict
- Small Arms Proliferation
- Riots and Protests
- Fatalities from Conflict
- Military Coups
- Rebel Activity
- Militancy
- Bombings
- Political Prisoners



Factionalized Elites

FE

When local and national leaders engage in deadlock and brinkmanship for political gain, this undermines the social contract.

Includes pressures and measures related to:

- Power Struggles
- Defectors
- Flawed Elections
- Political Competition



External Intervention

EXT

When the state fails to meet its international or domestic obligations, external actors may intervene to provide services or to manipulate internal affairs.

Includes pressures and measures related to:

- Foreign Assistance
- Presence of Peacekeepers
- Presence of UN Missions
- Foreign Military Intervention
- Sanctions
- Credit Rating

Thailand's Fragile State Index in comparison (2014): 77.0

Fractionalized Elites: 9.5

Human right: 7.4

Legitimacy of state: 7.1

Fragile States Index 2014		Total	Demographic Pressures	Refugees and IDPs	Group Grievance	Human Flight	Uneven Development	Poverty and Economic Decline	Legitimacy of the State	Public Services	Human Rights	Security Apparatus	Factionalized Elites	External Intervention
80	Thailand	77.0	7.6	6.5	8.0	3.8	6.1	3.6	7.1	4.9	7.4	7.9	9.5	4.6
117	Malaysia	66.2	5.5	4.5	6.2	4.8	5.6	3.9	6.6	4.6	6.9	6.5	7.0	4.1
160	France	34.8	3	2.5	6.4	2.2	4	4.5	2.1	1.8	2.2	2.6	1.9	1.6
176	Denmark	22.8	2.8	1.4	3.4	2.0	1.8	2.2	0.8	1.7	1.6	1.8	1.4	1.9

Why Nations Fail

- Daron Acemoglu and James Robinson (AR)
- Book Reviews by William A. McCleary in Thammasat Economic Journal, 31(1) March 2013
- **Rejection** of three alternative explanations of why experiences of various countries has been different: Geography, culture, and ignorance of correct policies.

Extractive institutions

- Nations are poor because they do not have institutions which allow them to generate growth potential.
- Political institutions in ***which power is heavily concentrated.***
- The extractive institutions do not create an environment in which ***a large proportion of population can share in the benefits.***

Inclusive institutions

- Political institutions in ***which power is widely shared and many groups*** can participate in the decisions which affect their prosperity and access to public services.
- Institutions that generate opportunities to invest, create new or better products, self-improvement.
- By securing property rights, an objective system of law, and limited monopoly privileges.

Examples of inclusive and extractive institutions

- England in the industrial revolution was an example of inclusive institutions
- The Glorious Revolution (1688): the king could exercise power only **with the consent of parliament** and made the government more responsive to a wider set of groups in society.
- Extractive societies of Soviet Russia and China which has experienced years of spectacular growth **could** slow down.
- The slowdown is now occurring in Russia and China.

How to measure quality of government

- Governance indicator
- Press freedom index
- Regulatory quality
- Political stability
- Voice and accountability
- Rule of law
- www.govindicators.org
- The Worldwide Governance Indicators (WGI) provided by the World Bank

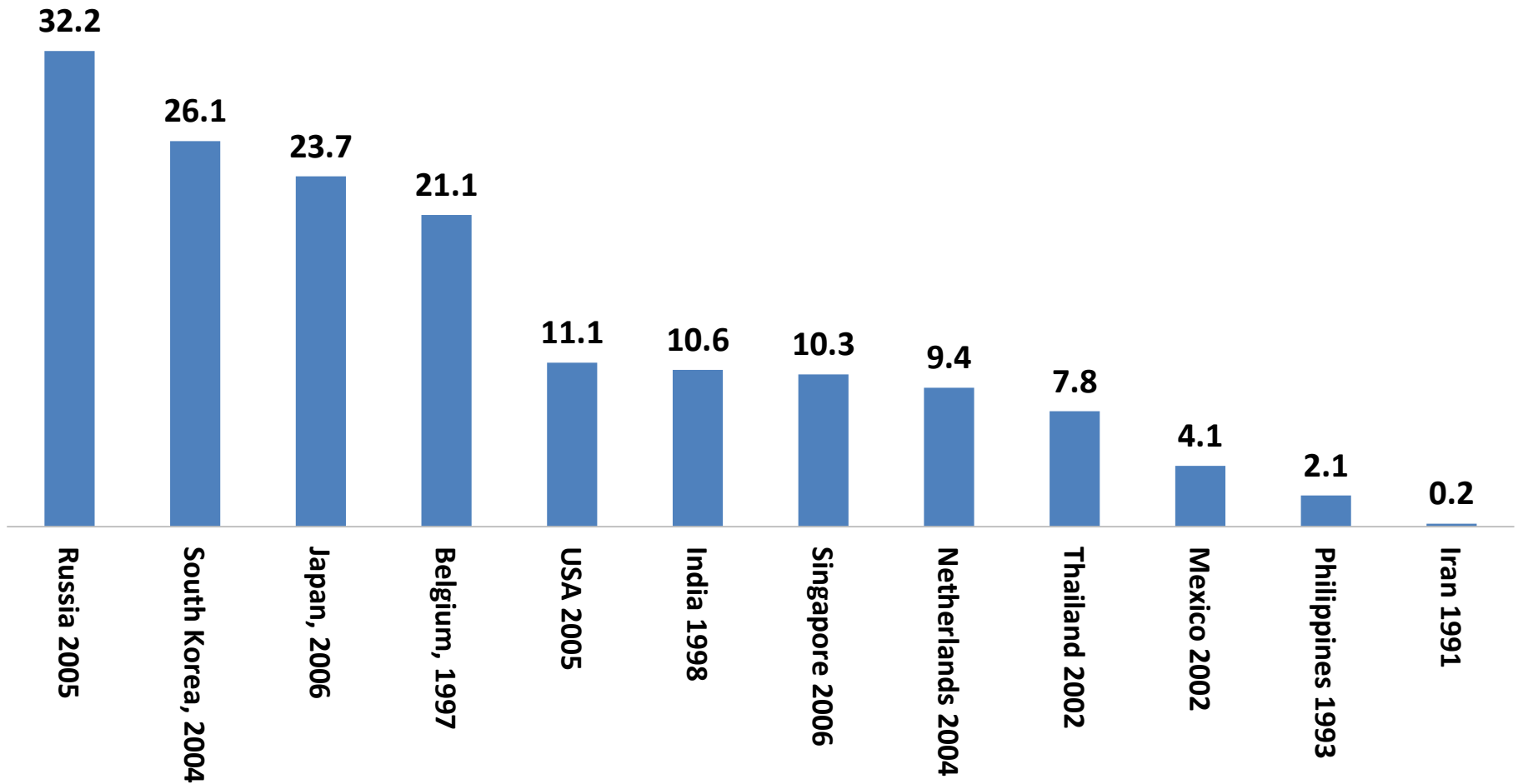
Can public policy make people happy?

- Public policy can more easily remove misery than augment happiness.
- To live happily is an inward power of the soul” Aristotle
- Hence, happiness depends on your **inner life** as much as on your outer circumstances.

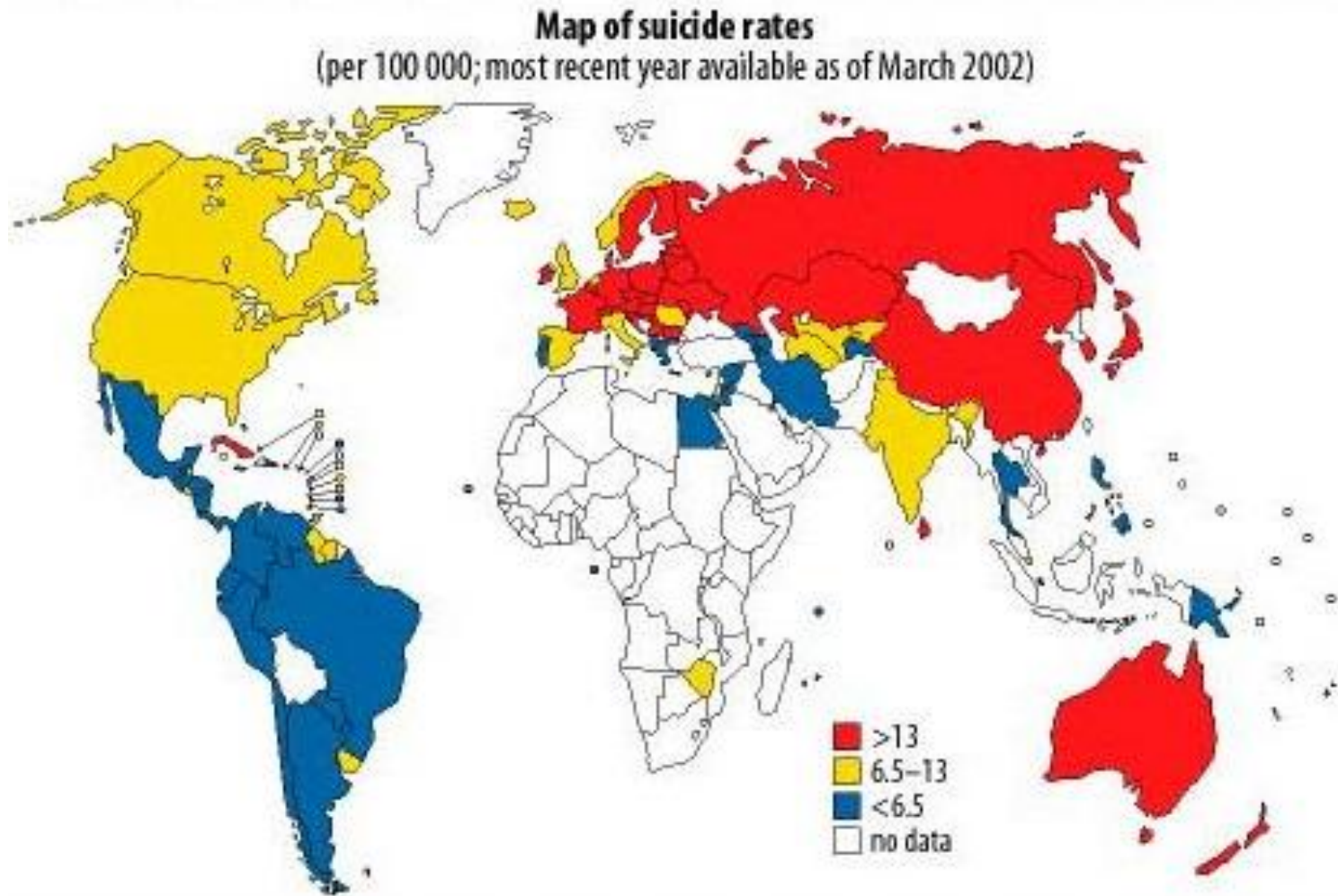
International suicide statistics

- Over one million people die by suicide worldwide each year.
- The global suicide rate is **16** per 100,000 population
- On average, one person dies by suicide every 40 seconds somewhere in the world.
- 1.8% of worldwide deaths are suicides.
- Global suicide rates have increased 60% in the past 45 years.

Number of suicides per 100,000 people, per year



Map of International Suicide Rates:



The 12th National Economic and Social Development Plan (2017-2022)

- Strengthen competitiveness
- Reduce income inequality
- Provide safety net for the ageing population
- Infrastructure development and logistics
- Special economic zones
- Cooperation with neighboring countries for greater connectivity
- Development of technology and innovation by increasing R&D expenditures (Thailand 4.0 Model)

Review questions

1. Explain how Thailand's economic development plans evolved around development theories and changing socio-political environment.
2. Utilize Layard's sources of happiness to examine the impact of economic development on happiness of the Thais over the past three decades.
3. Select two development plans that you think they had provided the most important contribution to the Thai economy. Provide evidence to support your arguments.
4. Can sufficient economy principle serve as immunization for a country under globalization?
5. Is Gross National Happiness (GNH) more superior than Gross National Product (GNP)?
6. Is there still any sign of economic backwardness in Thailand in 2017? Are we ready for Thailand 4.0 model of development?