Making Growth Deliver Exports – Not the other way around

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Suddenly, it seems, the momentum has shifted. For most of the past decade, the developing world was growing at a much faster clip than the rich North, creating talk of a new international world order, an "Asian century" and generating much hype about the emergence of the BRICS. The global financial media pushed these ideas even further, talking about the huge economic potential about to be unleashed particularly in those developing countries that still had relatively low per capita incomes and predominantly young populations.

These claims were repeated so constantly, and the euphoria thus created was so widespread, that governments in many developing countries could be forgiven for falling into the trap of believing this wholesale. And so many forgot that they still had a very long way to go and many internal and external structural constraints to overcome before they could simply "arrive" on the world stage as major and resilient economic powers. They also took the easy way out in terms of looking at aggregate growth rates rather than the pattern and structure of growth. As a result, they often failed to notice when rapid economic expansion was simply the result of bubbles being formed on the basis of volatile capital flows; or when excessive reliance on hot money inflows or on some primary commodity exports simply generated higher incomes for a minority of the population without improving the conditions of living of the majority; or when the growth trajectory was associated with unsustainable ecological damage, displacement of people and loss of livelihood without creating better new jobs.

All it has taken is a year or so of slower export growth and some movements of volatile capital flows back to the perennially "safe" destinations like the US, to bring on a harsh reality check. So now the pendulum of "market opinion" and "investor confidence" has swung in the opposite direction. Suddenly the same countries that could do no wrong in the eyes of global investors can do no right. World exports have slowed down considerably because of the slowdown in the North, but more to the point there are also greater efforts at curtailing both fiscal and external imbalances in the rich countries, so that demand from the developing world is adversely affected. Global capital is now shunning most of the countries that were the favourite destinations just a couple of years ago, with the main exception being China, whose continuing and huge current account surpluses give it a position of almost unassailable external strength.

As part of this process, the truth that always lurked behind the smoke and mirrors of the boom period is being dragged out into public view, to loud exclamations of shock and horror. The worst afflicted are countries like India and Indonesia, whose exchange rates and stock markets have been battered in the past months. Global media are rediscovering to their apparent surprise that these are mostly poor countries, with poor infrastructure, poor levels of health and education, poor interlinkages across sectors and regions, and lots of poor people. The "crony capitalism" and corruption that actually powered the earlier growth and enabled and even facilitated a large part of the multinational investment is decried and shunned. The massive attacks on working people (through displacement, loss of livelihood, terrible working conditions, low wages, completely inadequate provision of basic needs) and the various forms of

social discrimination and exclusion that the accumulation process used to its advantage when it suited, are now regularly covered in "exposes" in global media. And the terrible social and political fallout of increasing inequality and material fragility that accompanied the growth process – more social tension, more violence (especially against women), more uncertainty in everyday life – are seen as reason enough to shun these countries without any recognition of how global capital was complicit in generating these, along with internal political economy features.

But it is pointless and really a waste of time for people in these developing countries to complain about the rapid change in financial market and other global attitudes and the injustice and oversimplification involved in either extreme characterisation. The point is, this is what is happening today, whether we like it or not. And so the type of global integration and the nature of capital flows that were the drivers of the earlier boom are now no longer likely or even possible. So what do developing countries do in the current context? How exactly do they get on with (or even properly start on) the actual work of developing?

The latest Trade and Development Report 2013 from UNCTAD provides some answers. The Report notes that developing and transition economies can no longer rely heavily on exports to developed nations at the same rates of expansion as earlier. Whether or not there is partial or mild recovery of growth in these countries, growth of consumer demand has already dropped considerably and there is more emphasis on reducing net import demand. While primary commodity producers may still benefit from continued growth in demand from China (even if at a slower pace than earlier) manufactured exporters are likely to face more problems.

One big reason for this is the nature of the export-led growth strategy in many developing countries. Even when producing manufactured goods for the world market drove the expansion of more modern sectors (both formal and informal), domestic demand mostly did not increase in pace with this. This was partly due to weak linkages between the export sector and the rest of the economy, which are also affected by the pattern of insertion into global production chains that develop only a small part of total production in a particular location. But it was also due to the strategy employed by companies and encouraged by governments, of keeping wages low so as to maintain or improve external competitiveness.

But the point is that low wages dampen domestic demand growth, especially when many other countries pursue the same strategy simultaneously. What appears to be beneficial for any one country then turns out to be bad for all countries together: wage and tax competition among exporting countries exacerbates the harm caused by slower growth in export markets.

So the way out of the current morass is not to continue on the same path, but instead to look at domestic demand growth as a major impetus for industrialisation. This was a central tenet of mid-20th century development theory but is often overlooked today. For manufactured goods exporters, this involves developing the linkages between export sectors and the rest of the economy, as well as orienting more production (including small scale production) to the likely demands of domestic consumers. For primary commodity exporters, it is obviously important to use their revenues from resource exports to diversify their economies. For both types of countries ensuring

that real wages grow along with labour productivity increases is important to ensure sustained demand increases.

In each country, this obviously requires an appropriate balance between household consumption, private investment and public expenditure, and the Report has much to say about the interlinkages between these and how each of them can be usefully and sustainably expanded. But a critical insight of the Report is that expanding domestic demand can also have significant positive implications for the development of productive capacities, innovation and technology development within the country, generating a more stable and sustainable virtuous cycle. Obviously this in turn requires active industrial policy, another thing that has only recently been rediscovered as absolutely crucial for development.

The main point is that development strategies that give a greater role to domestic demand as the primary impetus for growth can be pursued by all countries simultaneously, without "beggar-thy-neighbour" effects and without competing by lowering taxes and wages in counterproductive fashion. If many countries do this simultaneously, they can in turn spur more South-South trade – which in turn can stimulate more export growth. So, in a neat inversion of the standard argument, this generates a process of growth-led exports, a process that could also be a more just and democratic one.

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