Productive Development for Equality and Growth

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Neoliberal policy orthodoxy in Mexico

- Macroeconomic stability (narrowly interpreted to mean low inflation)
- Free trade (NAFTA, TPP)
- No regulation of foreign investment, especially FDI (foreign direct investment) (NAFTA, TPP)
  - Strong protection of foreign investors through the ISDS (investor-state dispute settlement) mechanism
- Strong protection of intellectual property rights (NAFTA, TPP)
- Social policy for the weakest (Oportunidad)

Neoliberal policies: The results I

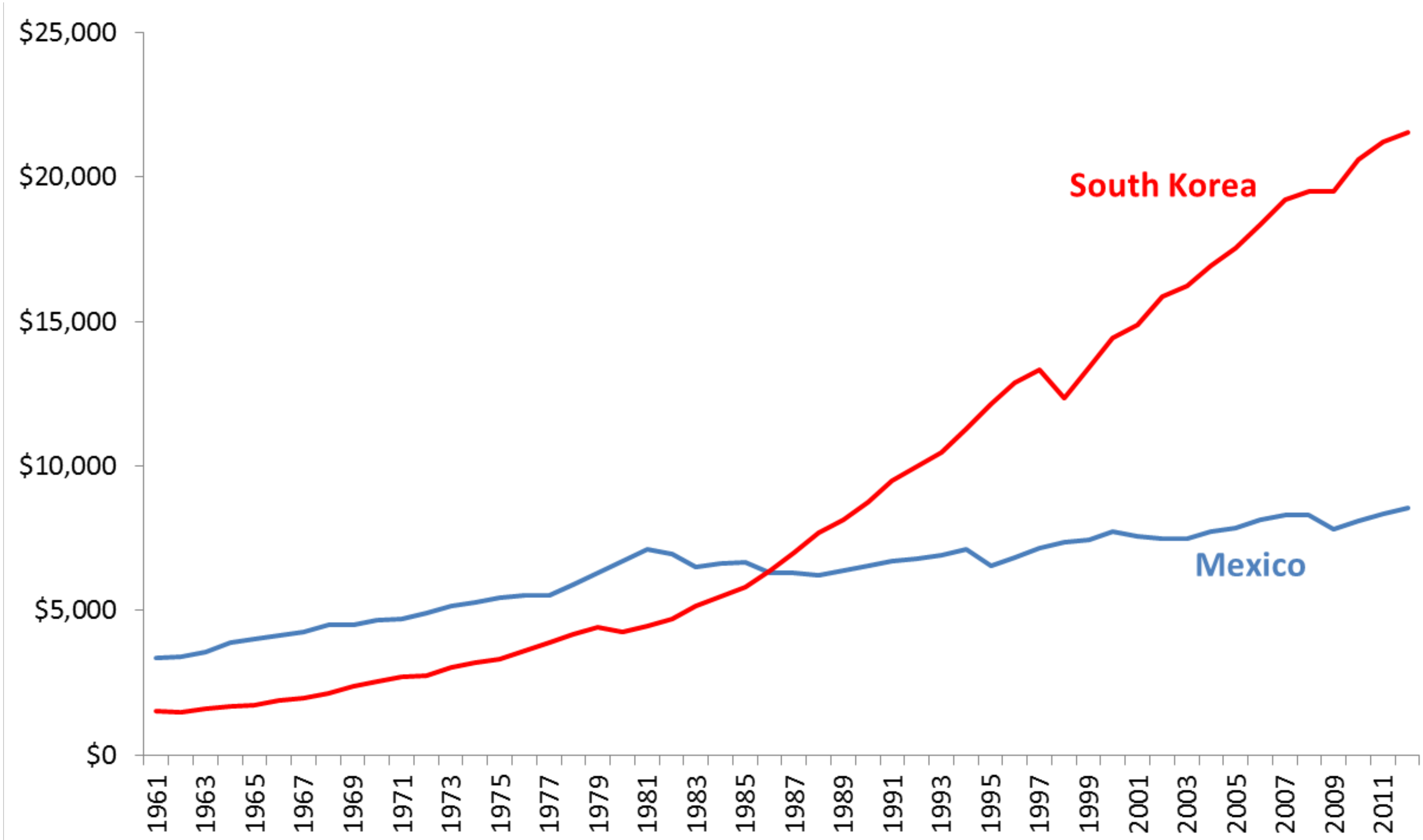
- Very disappointing economic growth
  - Between 1982-2017, Mexican GDP per capita in real terms (in 2010 US dollar) grew only at **0.6%** per year
  - Even in the post-NAFTA era of 1994-2017, growth rate was only marginally higher at **0.86%** per year

- This is much lower than what the countries had achieved during the ‘bad old days’ of import substitution industrialisation (ISI)
  - Per capita GDP in Mexico grew at **2.7%** per year between 1930 and 1982, that is, **4.5 times** faster than 1982-2017 and **3 times** faster than in 1994-2017

Neoliberal policies: The results II

- **Falling behind**
  - Compared to **the World**
    - In 1982, Mexican per capita income (current dollars) was **102%** of world per capita income ($2,542 vs. $2,502)
    - In 2017, it was **82%** ($8,910 vs. $10,748)
  - Compared to **the US**
    - In 1982, Mexican per capita income was **18%** of the US income ($2,542 vs. $14,439)
    - In 2017, it was **16%** ($8,910 vs. $59,927)
  - But when compared to countries like **South Korea** ….
    - In 1961, Mexican income was **382%** that of Korea's (Korea $94 vs Mexico $359)
    - In 1982, It was **129%** ($2,542 vs $1,978)
    - In 2017, it was only **30%** ($8,910 vs $29,743)

Mexico vs. Korea
(Per Capita GDP, constant 2005 US$)



Data source: World Bank's World Development Indicators 2013

Neoliberal policies: The results III

- Inequality has persisted
- Unlike in many other countries around the world, income inequality in Mexico has *not* significantly risen during the Neoliberal period
- However, the decreasing income inequality in other Latin American countries in the recent period has made Mexico one of the more unequal countries in Latin America

Neoliberal policies: The results IV

- Moreover, Mexico is the most unequal country in the OECD (occasionally swapping places with Chile)
  - Gini coefficient* for Mexico in 2016 was 0.46
  - the US (the most unequal amongst the richest OECD countries 0.39
  - South Korea 0.35; Spain 0.34; Portugal 0.33; Italy 0.30
  - Non-Mediterranean European countries 0.25-0.30

*complete equality is 0 and complete inequality is 1

Neoliberal policies: The results V

- Particularly worrying is the lackluster performance of the manufacturing sector, which was supposed to be boosted by the NAFTA

- Once upon a time, Mexico was one of the most industrialised nations outside the ‘core’ capitalist world
  - In 1961, per capita MVA (Manufacturing Value-Added) of Mexico (in 1958 dollars) was $83
  - Lower than only those of South Africa ($138) and Argentina ($114) and 37% that of Japan ($227), although only 9% that of the US ($926)
  - It was **1.7 times that of Brazil** ($50) and **3.8 times those of Korea** ($22) **and Taiwan** ($23)

Neoliberal policies: The results VI

- The share of manufacturing in GDP has shrunk
  - around 20% in the 1980s, but 15-17% since the early 2000s
- Declining international position
  - Mexico's manufacturing output (MVA: manufacturing value-added) per capita is *not* stagnant, unlike in **South Africa**, or *not* shrinking, unlike in **Brazil**
  - But its **relative position with China** has been recently **reversed** (30% higher in 2010, but 30% lower in 2015)
  - **Relative position with Korea** has been **dramatically reversed** (from 3.8 times in 1961 to 22% in 2015) in the last six decades
- The most important reason behind this relative decline of manufacturing is the failure to upgrade beyond the 'maquila' structure

Manufacturing Value Added Per Capita, 2015

(in constant 2010 US dollars; index USA=100)

- Switzerland $14,404 278 (world ranking: 1)
- Singapore $9,537 184 (2)
- Germany $9,430 182 (3)
- Sweden $8,568 166 (4)
- Japan $8,496 164 (5)
- Austria $8,338 161 (6)
- Korea $7,336 142 (7)
- USA $5,174 100
- China $2,048 40
- Mexico $1,593 31
- Brazil $1,203 23
- South Africa $952 18
- India $298 6

Source: UNIDO, *Industrial Development Report, 2016*

*Excludes Ireland, whose 'tax haven' status makes the 'booked' MVA fluctuates wildly

What to do? I

- Neoliberalism has greatly **worsened economic performance**, including economic growth, equality, and financial stability, everywhere

- But its performance has been **particularly poor in Mexico**

- Without completely over-turning the Neoliberal economic orthodoxy, Mexico’s future is bleak

- Indeed, this rejection of the Neoliberal paradigm is one of the things that have brought the current government into power

What to do? II

- At the most general level, what needs to be done is clear
- You have to promote the development of **national productive capabilities** in sectors that have dynamic technology, expanding demand, and dense 'linkages' with other sectors **through active industrial policy,** using:
  - **'Infant industry' protection** from superior foreign producers (tariffs, quotas, non-tariff barriers, bans)
  - Provision of **affordable, long-term finance** for investments (development banks, 'directed credits')
  - **Regulation of FDI** to encourage the accumulation of domestic productive capabilities (technology transfer, local contents requirements, worker training requirements)

What to do? III

- … development of **national productive capabilities** in sectors that have dynamic technology, expanding demand, and dense 'linkages' with other sectors **through active industrial policy,** using:
  - Strategic use of **SOEs** (22% of GDP in Singapore, 16% in Taiwan; also actively used by France, Austria, Finland, Norway)
  - Active **procurement policy** to help domestic firms (Japanese mainframe computer, Nokia in Finland, US aircraft industry)
  - Public provision, public-private joint investments, or subsidies to increase investments in **infrastructure, R&D and skills training**

What to do? IV

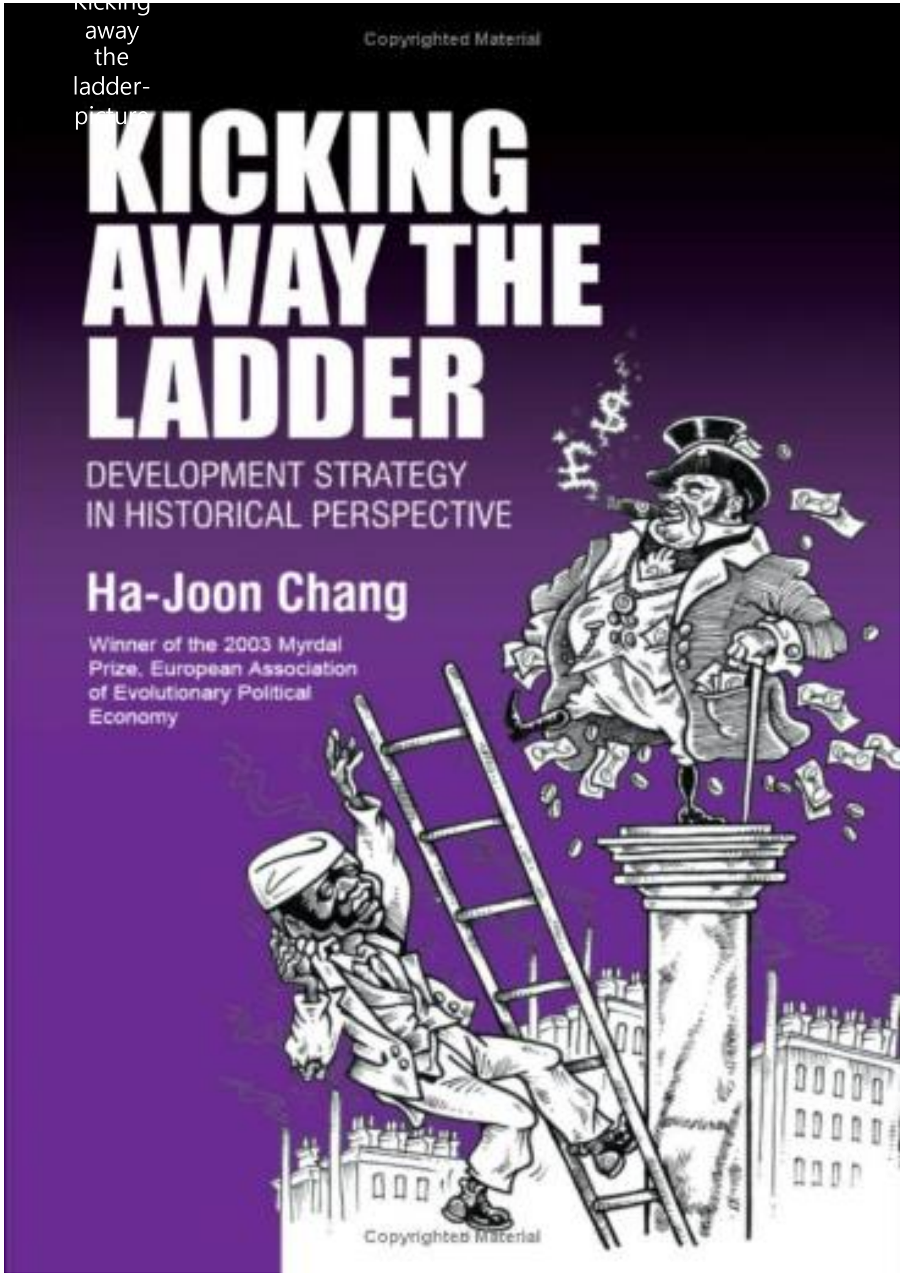
- In order to create a more humane society and make economic development politically more sustainable, inequality needs to be reduced
- This requires expanding the welfare state
  - Mexico has literally the smallest welfare state in the OECD
    - Mexico's welfare spending is 7.5% of GDP (2016)
    - Chile and Korea around 11%; US 18%
    - OECD average 20.1%
    - France, Belgium, Finland, Denmark 28-31%
- This also means reducing regional disparities
  - Subsidies to address regional disparities are allowed even by the WTO

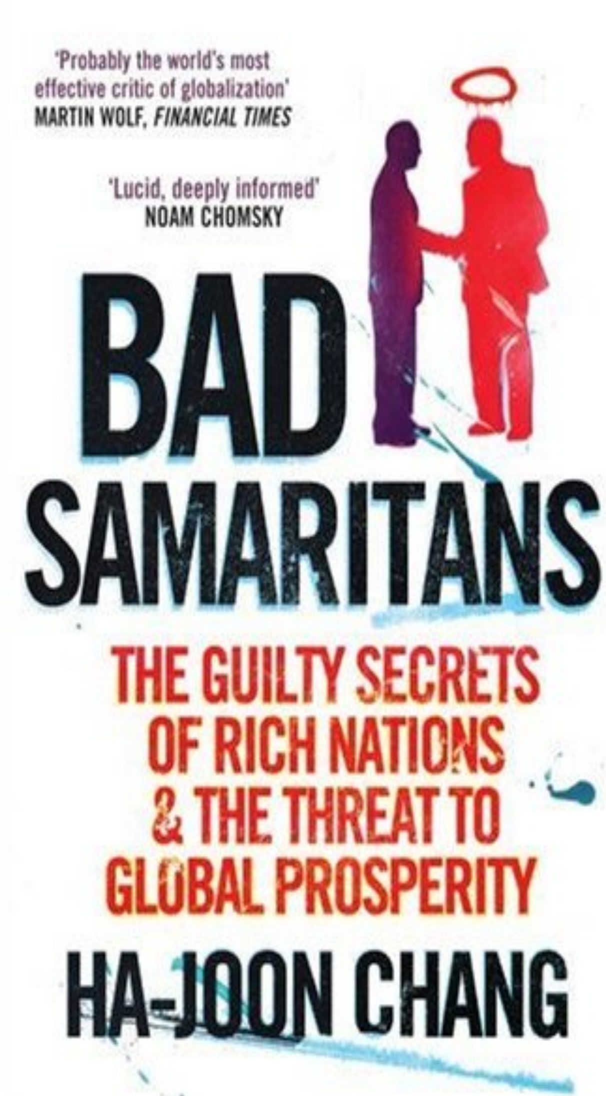
What to do? V

- And these are indeed the policy measures used by the more successful economies in order to promote economic development in the last three centuries
  - 18th century: Britain
  - 19th-early 20th century: the US, Germany, Sweden, Belgium
  - Late-20th century: France, Austria, Norway, Finland, Italy, Japan, Korea, Taiwan, and Singapore **(US again but with a different emphasis – massive funding and subsidies for R&D in hi-tech industries)**
  - Today: China

- And indeed, these (except the welfare state) are policies that Mexico had used, albeit now as effectively as did those other countries, during its ISI period

Kicking away the ladder-picture

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What to do? VI

- Of course, all of this does not mean that you can simply copy what other countries did

- Different countries have used different policy combinations, because they faced different conditions and had different ambitions **(e.g., automobile)**

- Also, the international conditions are different from the past
  - Shrinking ‘policy space’ (WTO, NAFTA, TPP)
  - The rise of the so-called Global Value Chain
  - The alleged rise of ‘post-industrial knowledge economy’

Shrinking Policy Space I

- There are many industrial policy measures that can still be used legally under the WTO
  - Some policy measures are inherently domestic in nature and thus not subject to international agreements
    - investment subsidies, targeted investment in infrastructure, subsidies for skills development, provision of subsidised consulting services by government agencies
  - There are subsidies that are challengeable in theory but are hardly ever challenged in practice
    - subsidies for R&D, upgrading of disadvantaged regions, and developing environmentally friendly technology
  - Some FDI regulations are still legal
    - Those related to joint venture, technology transfer, or limitations on foreign equity ownership

Shrinking Policy Space II

- However, bilateral and regional agreements like NAFTA and TPP are much more restrictive than the WTO, so Mexico's policy space is more limited than countries that are only members of the WTO.

- Therefore, Mexico needs to put in more effort in finding ways to get around the restrictions imposed by NAFTA and TPP.

The Expansion of Global Value Chains I

- After NAFTA, Mexico has successfully inserted itself in some important global value chains (GVCs) – cars, electronics, textile and garments.

- Unfortunately, much of these maquila industries have been lost to China and other Asian countries, except in the automobile sector.

- And the insertion into GVCs has led to the decline of domestic intermediate inputs producers, as TNCs usually import most of their inputs

The Expansion of Global Value Chains II

- Mexico's own experience show that, unless it is done as a part of a well thought-out industrial policy strategy, GVC participation can actually harm developing economies, especially in the long run.

- Therefore, Mexico needs to introduce measures to help its producers upgrade within GVCs and eventually to create and control their own GVCs (e.g., Korea electronics)
- This, in turn, requires intelligent industrial policy, as indeed shown by the experiences of the East Asian countries (not just Korea, Taiwan, but also China, Singapore)

‘The post-industrial Knowledge Economy’? I

- We have always lived in a knowledge economy.
  - It was never the act of making things but the control over superior productive knowledge that has been the key to economic prosperity.

- Many knowledge-intensive services (e.g., research, engineering, design, consulting) that are supposed to be new have always been there.
  - Most of them used to be conducted by manufacturing firms themselves and became more ‘visible’ recently mainly because they have been ‘spun off’ or ‘outsourced’.

‘The post-industrial Knowledge Economy’? II

- Manufacturing has always been the main source of productive knowledge.
  - Manufacturing lends itself much more easily to mechanisation and chemical processing, so it is much easier to raise productivity in manufacturing than in agriculture or services.
  - Manufacturing is also the sector where most R&D is conducted.
    - Even in the US and the UK, where manufacturing accounts for only around 10% of GDP, 60-70% of R&D is conducted in the manufacturing sector.
    - The ratio is 80-90% in Japan, Germany, and Korea

‘The post-industrial Knowledge Economy’? III

- Manufacturing enables productivity growth in other sectors by supplying inputs (e.g., fertilisers, computers) and organisational innovations (e.g., inventory management technique, computer-controlled feeding).

- Most of knowledge-intensive services (finance, design, and engineering) are mainly sold to manufacturing firms, so their success depends on manufacturing success.