Lecture 7: International Institutions

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Finishing Discussion of China

- What can we learn from previous growth experiences for the future of China?
- Comparison to the case of Mexico
- After that, move on to talk about international institutions
Growth Experiences

- China’s growth rate, even over such a long period of time, is not uncommon

- Things to notice from other growth experiences:
  - Countries typically grow for a long time, then stop
  - How long their growth lasts varies widely
  - The growth slowdown is typically sudden (unforeseen)
  - Usually the slowdown comes in the form of a recession (negative growth)
  - Countries stop growing before they “catch up” with the US
What is China’s Future?
Extrapolating China’s Future: per capita

Crossing in 2041
Extrapolating China’s Future: Levels

$128,000,000,000
$64,000,000,000
$32,000,000,000
$16,000,000,000
$8,000,000,000
$4,000,000,000
$2,000,000,000
$1,000,000,000
$500,000,000
$250,000,000


China
USA

Crossing in 2025
More Serious Estimate: per capita

Not Crossing

Taiwan
China
Hong Kong
Korea
Singapore
Macao
Japan
USA
“Catch up”

- This phenomenon of the rate of growth slowing as the country approaches the highest GDP per capita levels is called the “catch up” effect.
- Formalize this next time.
- Conceptually, growth comes from two places:
  - Gains from improved policy
  - New technology
- The richest countries only gain from new technology, fast growing countries are gaining from both.
- Once all gains from improved policy are exhausted, then just grow with technology.
- Mexico and China

- Kehoe and Ruhl (2010)
- Mexico improved policy and experienced decades of fast growth
- Growth ended suddenly in a crisis in 1994
- Has not continued since
- Conceptually: had SOME policy reforms that were effective for a while
- However, never fixed important underlying reforms, which ultimately limited growth
- China: needs to continue reforming policy to continue growth
World Institutions

- There are a variety of international institutions that are designed to pursue international growth and stability
- We will focus on three:
  - World Bank
  - International Monetary Fund (IMF)
  - World Trade Organization (WTO)
- All three have a stated goal related to promoting the growth and stability of developing countries
- What do they do?
- Are they any good at it?
What Can the International Community Do about Poverty?

- Up to now, we have always considered the problem of a government trying to reduce poverty.
- What if you are an outsider?
- Take into account: not all governments are purely benevolent.
- What types of things should be done to encourage them to grow?
Purview of Each Institution

- World Bank:
  - Long Term loans
  - Encourage infrastructure or other large scale projects

- IMF:
  - Short Term loans
  - Maintain stability of currency values

- WTO:
  - Encourage trade among nations
  - Provide mechanisms for trade negotiation and resolution of trade disputes
History of these Institutions

- All three came into existence in 1944
- 44 nations met at the “Breton Woods” conference (UN Monetary and Financial Conference)
  - Took place at the Breton Woods Mountain Resort in New Hampshire
- Questions for the conference:
  - How to keep out of another Great Depression?
  - How to rebuild Europe?
  - How to avoid a repetition of the Treaty of Versailles?
  - How to maintain stability?
Original Goals

- Solution: Three international organizations
- World Bank: Provide structural loans for infrastructure
  - Originally meant to help rebuild war-torn countries
- IMF: Provide short term loans to stabilize currencies
  - Meant to maintain currency balance in system based on US dollar stability
- WTO (originally GATT): Facilitate trade
  - Provide international trade mechanism
World Bank

- Based in Washington, DC; always headed by an American
- Makes very large loans with long durations
  - Example: $500 million loan to Vietnam to improve electricity transmission in 2014
- The funds are paid in by member states, they receive interest on those funds
- Loans come with “strings attached” called “structural adjustment programs”
- Provide training for government officials in developing countries
International Monetary Fund

- Also based in Washington, DC; always headed by a European
- Makes loans with short durations during crises
  - Example: $17 billion loan to Ukraine in 2015
- The funds are also paid in by member states
- Loans come with “strings attached” called “structural adjustment programs”
- Often opens “lending facilities” as a sort of line of credit to head off crises
  - Example: Mexican financial crisis in 1994
World Trade Organization

- Originally called GATT (1944-1994)
- Member countries must simplify trade protections
- Give all other member nations “Most Favored Nations” status
- Has 157 members (largest non-member: Iran)
- Provides arbitration for trade disputes
- Provides for facilities to negotiate bilateral tariffs
- Encourages reductions in “non-tariff barriers”
Structural Adjustment Programs

- Both the IMF and World Bank require these as conditions for loans
- Examples:
  - Fiscal Austerity: Raise taxes and/or cut spending
  - Remove wage/price controls
  - Privatize industries
  - Open to international trade and capital
  - Reduce corruption
Structural Adjustment Programs

- These programs are targets of harsh criticism
- Main critiques:
  - Advice typically isn’t narrowly tailored
  - Effectiveness: Not much evidence that they’ve increased growth overall
  - Indebtedness: Countries may end up with big debts and not be able to repay
  - Immunity: The World Bank cannot be sued, as a requirement of taking the loans
Criticism of Globalization

- The WTO is a target of “Anti-Globalization” criticism
- Globalization: The ongoing process of increased integration of the world economy

Criticisms:

- “Race to the Bottom”: International competition to be the lowest cost producer leads to bad outcomes for workers and the environment
- Rights of Domestic Workers: Competition with workers of low wages in other countries reduces domestic wages
- Financial Market Instability: Lack of restrictions on movements of capital flows allows for “capital flight”
The Case of India

- India has had a centrally managed economy for most of its history.
- This led to very slow growth and widespread poverty.
- In 1991, India had an exchange rate crisis that required an IMF loan. This led to:
  - Privatization
  - Labor reforms
  - Inflation controls
- Subsequently, the Indian economy has grown for 20 years at very fast rates.
- This is just one example!
Do these institutions do harm or good?

- In India, they seem to have undoubtedly helped
- In general, the evidence is mixed

Questions:

- Should these institutions be abandoned completely?
- How can they do their job better?
  - Probably need to have a better understanding of the country they are advising
  - Work harder to identify the policies that seem to work and promote those, rather than general free market principles
Next Lecture

- Last topic on growth: labor markets
- Midterm next Thursday
- Midterm study material posted online