

Public Lecture

Uzbekistan:

New Strategies and Opportunities for Structural Transformation

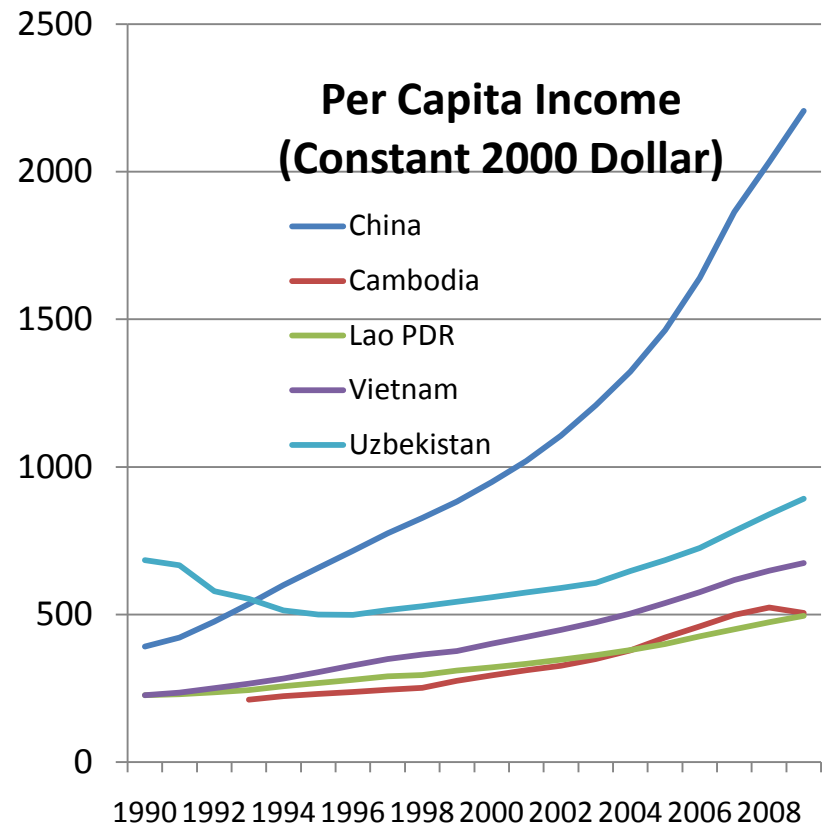
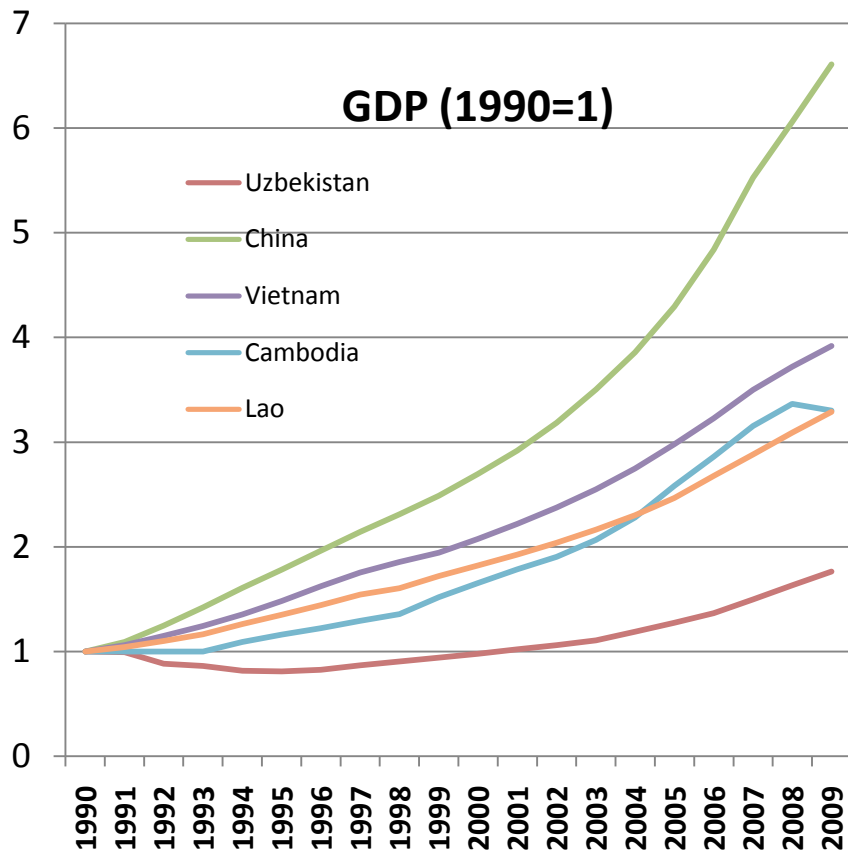
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The World Bank

Tashkent, July 7 2011

However, compared to the transition economies in East Asia, Uzbekistan's economic performance can be further improved:

-- The annual GDP growth rate in China, Vietnam, Cambodia and Lao in 1990-2009 reached 10.4%, 7.5%, 7.7% and 6.5% respectively.

--In 1990, China's per capita was half of Uzbekistan's, it increased to 2.5 times of Uzbekistan's in 2009.



Purpose of the presentation

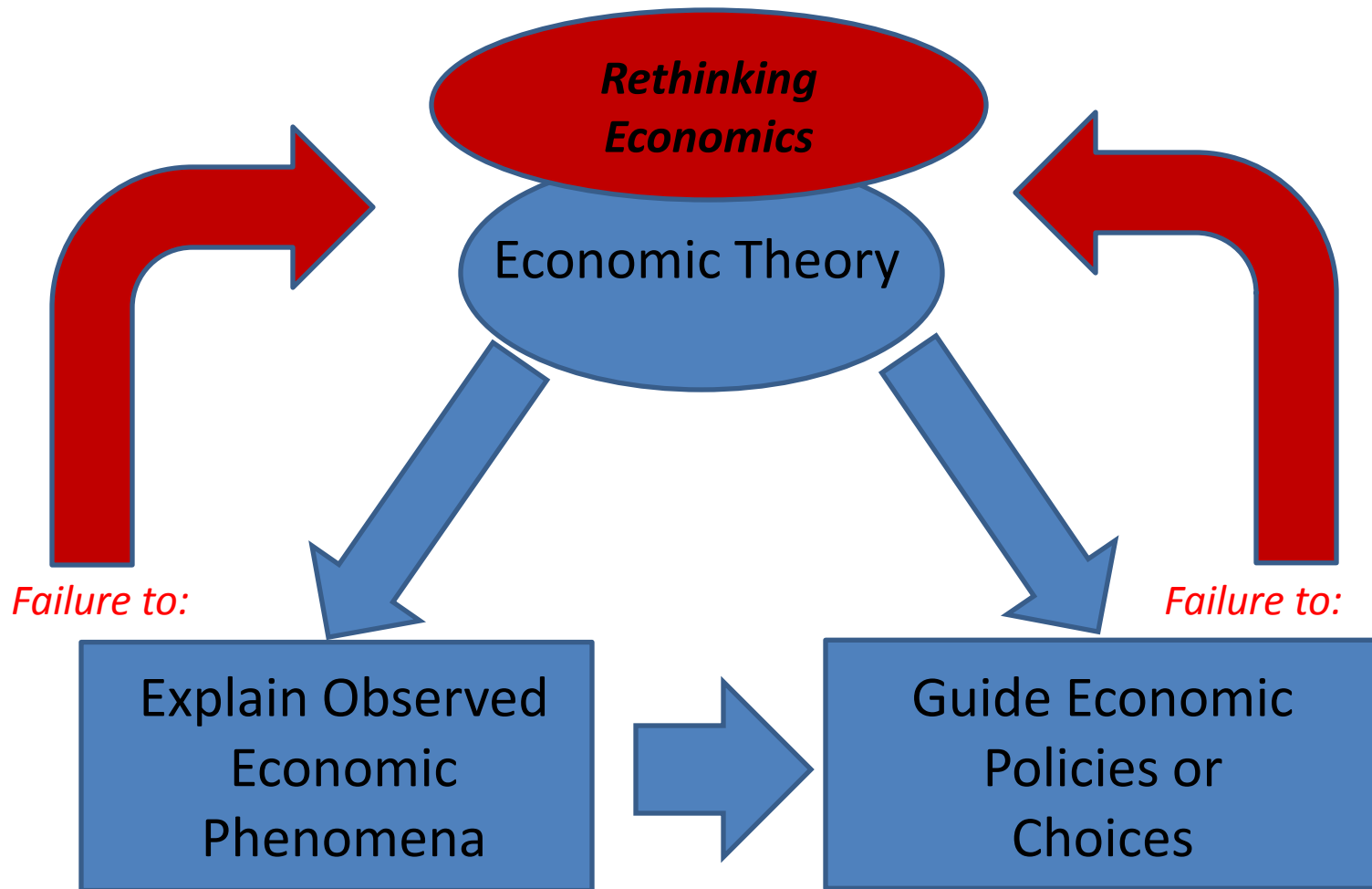
- I believe that every developing country in the world has the potential to grow at 8 or more percent annually continuously for several decades, avoiding the middle-income trap, and becomes a high-income country within one or two generations
- As long as the government's policy is right and is implemented well, Uzbekistan's goal of becoming an industrialized high middle-income country by mid century can be achieved or even out performed
- I hope to share some new insights about how a developing country can tap into its growth potential and contribute to the policy discussions in Uzbekistan

Overview of Presentation

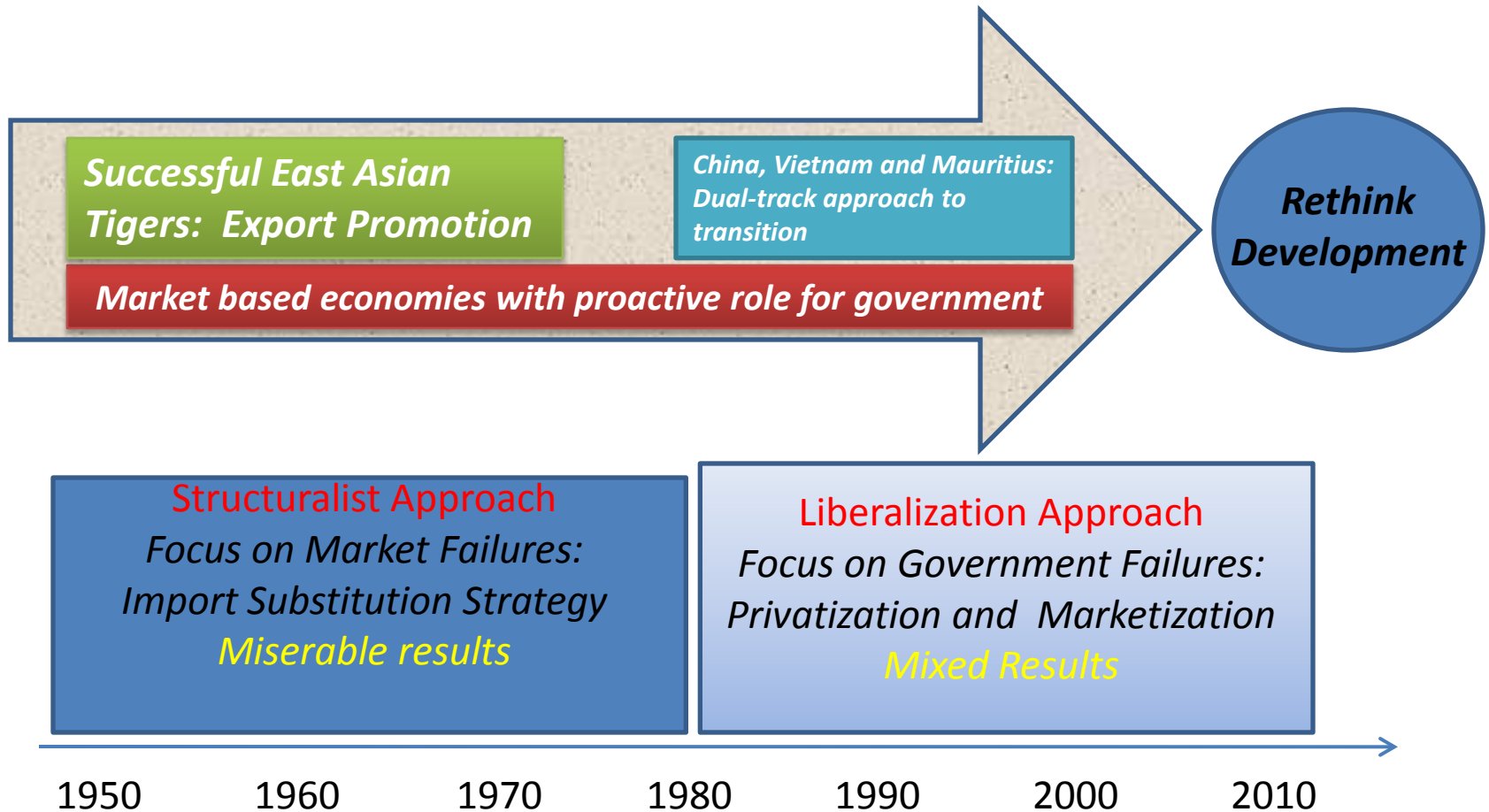
- The need for rethinking development
- The New Structural Economics
- The Growth Identification and Facilitation: An application of new structural economics
- The New Opportunities for Uzbekistan in the Multi-polar Growth World
- Concluding remarks

WHY DO WE NEED TO RETHINK DEVELOPMENT

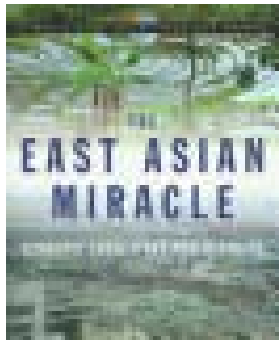
Economic Crisis and Crisis in Economics



How has economic development theory evolved?



World Bank has been in the process of rethinking economic development



Export
Orientation and
Market Friendly
Government



No one-size fits all



- (i) Openness;
- (ii) Macro stability;
- (iii) High rates of saving & investment;
- (iv) Market mechanism;
- (v) Committed, credible & capable government

THE STRUCTURAL ECONOMICS

Introducing...

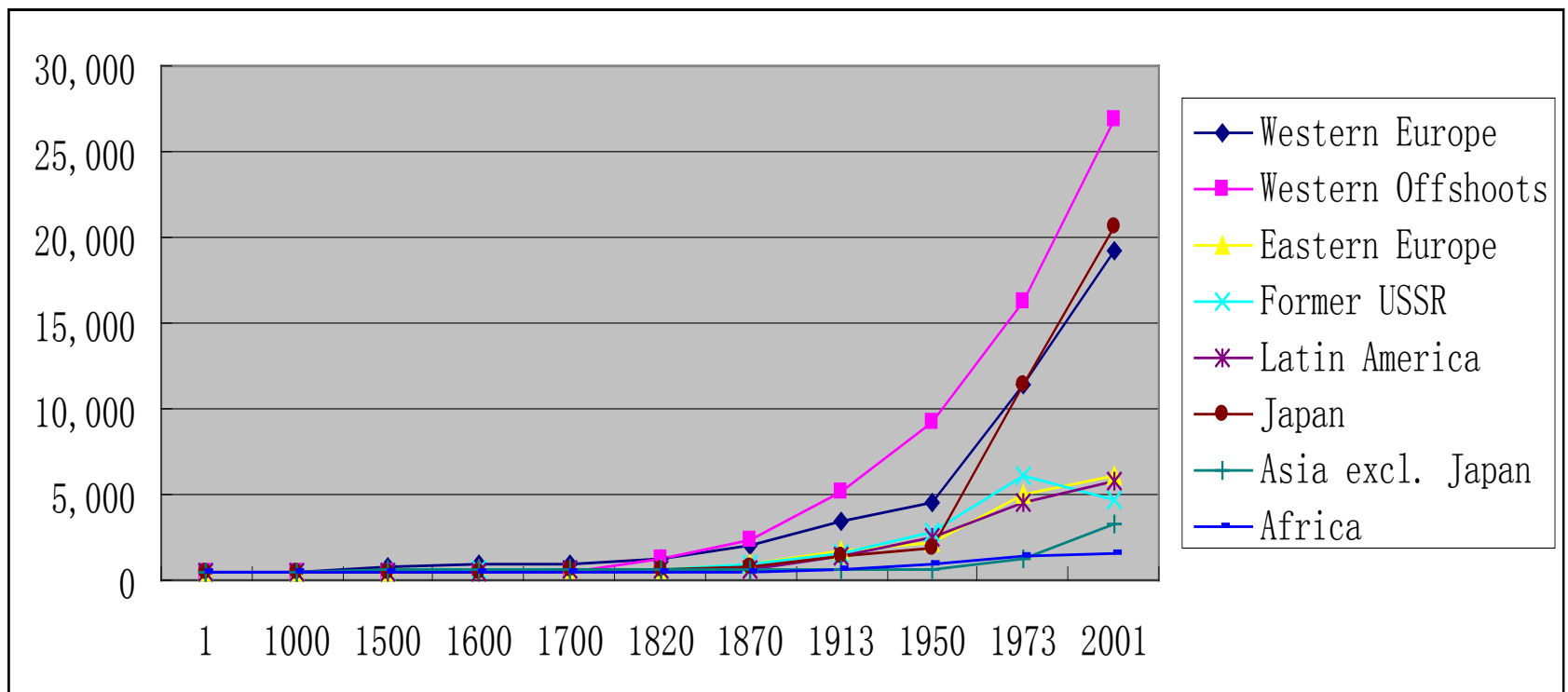
New Structural Economics

- Application of neoclassical economic approach to understand changing **economic structure** in development
- Provides a consistent framework for the **five stylized facts** of *Growth Report* as well as the findings from the *East Asian Miracle*
- Contributes to **new theoretical and policy insights** for economic development

Introducing...

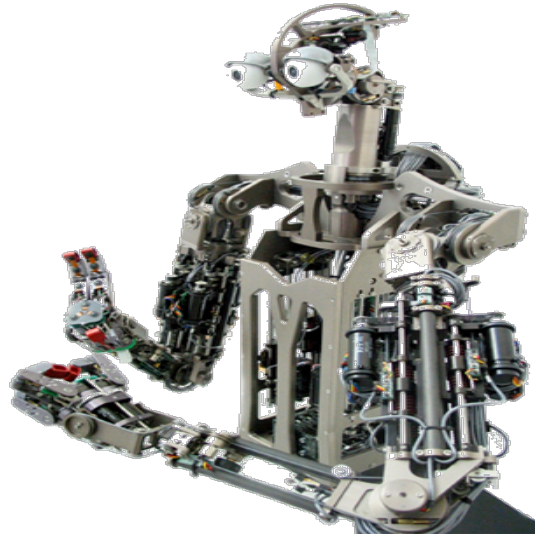
New Structural Economics

- *Sustainable income growth is a recent phenomenon*



- *The sustainable income growth is a result of continuous technological innovation **as well as structural change***

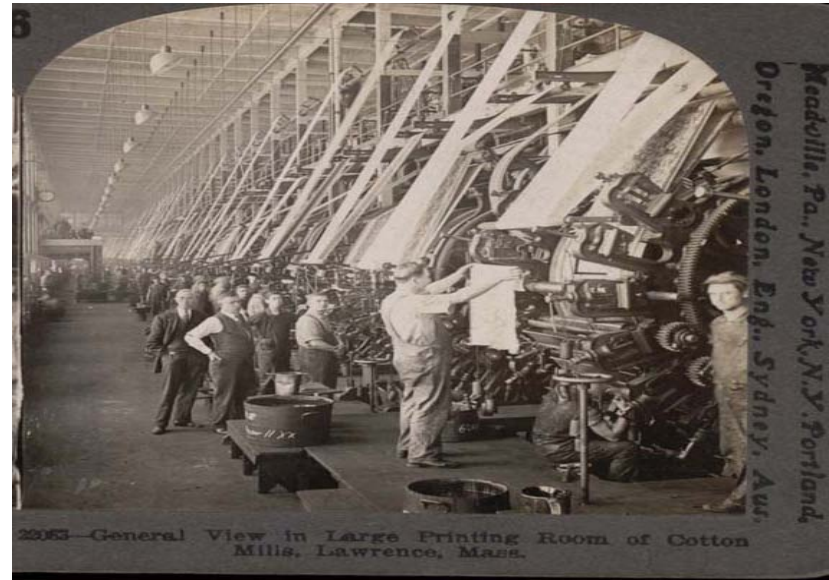
Example: USA, Now



Industrial Structure in New England, 1600s



Industrial Structure in New England, 1800s



SPECIALTIES.
 as light, fine shoes manufactured by the
BOSTON SHOEING BRICK COMPANY





Weight and quality guaranteed by this Company and received
 international, or where better the quality of "Boston" shoes.
 The names of these styles, they are all packed in cartons.

<p>Men's LIGHT RESPECTABLE (Black Upper, Wood Sole)</p> <p><small>The above style is made of black leather, with a light sole, and is well known.</small></p>	<p>Men's LIGHT RESPECTABLE (Black Upper, Rubber Sole)</p> <p><small>A fashionable style, with which all the military regiments, etc., are supplied.</small></p>		
			
			
<small>Pringle</small>	<small>Windsor</small>	<small>Windsor</small>	<small>Windsor</small>

The above styles are made from the finest of the
 lightest and most durable leather, with
 light, rubber, or wood soles, and are
 made in the best manner. The name of these
 styles are shown above.

For a Complete List of Styles of These and Men's and Women's Shoes, see page 11 and 12.

New Structural Economics (NSE): Key Concepts

- The main hypothesis: Industrial structure is endogenous to endowment structure
- Initial Endowments (determine the economy's total budgets and relative factor prices at time t) 
 - Comparative advantage 
 - Optimal industrial structure (endogenous).
- Dynamics: Income growth depends on
 - Upgrading of endowments 
 - Upgrading industrial structure 
 - “hard” and “soft” infrastructure
- *Following comparative advantage determined by the endowment structure to develop industries is the best way to upgrade endowment structure and to sustain industrial upgrading, income growth and poverty reduction.*

New Structural Economics (NSE): Key Concepts (2)

- Firms maximize profits...choice of technology and industries based on relative factor prices...

 *Need for competitive market system*

- Industrial upgrading needs to
 - Solve coordination problems
 - Form clusters
 - Address externalities

 *Need for a facilitating state*

NSE and The Growth Commission's Stylized Facts

Growth Report

Stylized Facts:

- Policy Recommendation from NSE
 - Following comparative advantage : Conditions
 - Market economy #4
 - Facilitating State #5
- The results:
 - Openness and advantage of backwardness #1
 - Competitiveness and strong external as well as fiscal accounts: fewer home-grown crises and larger scope for countercyclical fiscal policies. #2
 - Large economic surplus and high returns to investment: high rate of savings and investment. #3
- The NSE's recommendations are consistent with the *East Asian Miracle's* findings.

NSE and the Failure of Structuralism

- The structuralism advised the government to develop industries which were too far advanced compared to their level of development and went against their comparative advantages
- The firms were non-viable in competitive markets and required government policy supports for their initial investment and continuous operations.
- This led to rent-seeking, corruption, and political capture.

Country	Industry	Time	Main producer at Time	Real GDP pc Latecomer Country	Real GDP pc Leading Country	Income Ratio Follower versus Leader
China	Automobile	1950s	USA	577	10,897	5%
DRC	Automobile	1970s	USA	761	16,284	5%
Egypt	Iron, Steel, Chemicals	1950s	USA	885	10,897	8%
India	Automobile	1950s	USA	676	10,897	6%
Indonesia	Ships	1960s	Netherlands	983	9,798	10%
Senegal	Trucks	1960s	USA	1,511	13,419	11%
Turkey	Automobile	1950s	USA	2,093	10,897	19%
Zambia	Automobile	1970s	USA	1,041	16,284	6%

Source: Author's calculations based on data from Maddison (1995).

NSE and the Failure of Washington Consensus

- All transitional economies started with the existence of many nonviable firms in old priority sectors due to their previous comparative advantage-defying development strategy.
- The Washington consensus failed to recognize the distortions were endogenous in responding to the needs of protecting nonviable firms in the priority sectors and advised the government to eliminate all distortions immediately, which caused the collapse of old priority sectors.
- The Washington consensus also opposed the government to play a proactive role for facilitating the firms' entry to sectors that are consistent with the country's comparative advantages
- The dynamically growing transitional economies adopted a dual-track approach:
 - The government continued to provide transitional supports to nonviable firms in the old priority sectors and removes distortions only when firms in those sectors became viable
 - The government facilitated private firms' entry to sectors that were consistent with the country's comparative advantage and were repressed before the transition

THE GROWTH IDENTIFICATION AND FACILITATION

The Recipe for dynamic growth in a developing country

- The recipe
 - Developing a country's industries according to its comparative advantages so as to achieve competitiveness domestically and internationally
 - Tapping into the potential of latecomer advantages to reduce the costs and risks of industrial upgrading and diversification
- The pre-conditions
 - Market economy
 - Facilitating state
- If a developing country institute the pre-conditions and follows the above recipe, it can grow at 8 or more percent annually for several decades, avoid the middle-income and catch up with the developed countries

Industrial Policy in a Market Economy

- Industrial policy is a useful tool for the state to play the facilitating role for industrial upgrading and diversification in a market economy:
 - Contents of coordination will be different, depending on industries.
 - The government's resources and capacity are limited. The government needs to use them strategically.
 - To facilitate formation of clusters and obtaining agglomeration effect

“Aim before you fire”

- The key lesson, from the new structural economics, is that for an industrial policy to be successful, it should target sectors that conform to the economy’s latent comparative advantage.
- But how to do it?

Successful Experiences From History

- Britain targeted the Netherlands' industries in the 16th and 17th century, its per capita GDP was about 70 % of Netherlands'.
- Germany, France, and USA targeted Britain's industries in the late 19th century, their per capita income were about 60 to 75 % of Britain's per capita GDP
- In Meiji restoration, Japan targeted Prussia's industries, its per capita GDP was about 40% of Prussia's. In the 1960s, Japan targeted USA's industries, its per capita GDP was about 40% of USA's per capita GDP
- In the 1960s-1980s, Korea, Taiwan, Hong Kong, and Singapore targeted Japan's industries, their per capita income was about 30% of Japan's per capita GDP
- In the 1970s, Mauritius targeted Hong Kong's industries, its per capita income was about 50% of Hong Kong's.
- In the 1980s, Ireland targeted information industries, its per capita income was about 45% of the USA's.
- In the 1990s, Costa Rica targeted memory chip assembly and testing, its per capita GDP was about 40% of that of Taiwan, which was the main economy in this sector.

Growth Identification and Facilitation

Step 1:

Find fast *growing countries* with a similar endowment structure and with about 100% higher per capita income. *Identify dynamically growing tradable industries* that have grown well in those countries for the last 20 years.

Step 2:

See if some *private domestic firms* are already in those industries (of which may be existing or nascent). Identify constraints to quality upgrading or further firm entry. Take action to remove constraints

Growth Identification and Facilitation

Step 3:

In industries where no domestic firms are currently present, seek FDI from countries examined in step 1, or organize new firm incubation programs.

Step 4:

In addition to the industries identified in step 1, the government should also pay attention to spontaneous self discovery by private enterprises and give support to scale up the successful private innovations in new industries

Growth Identification and Facilitation

Step 5

In countries with poor infrastructure and bad business environment, special economic zones or industrial parks may be used to overcome these barriers to firm entry and FDI and encourage industrial clusters.

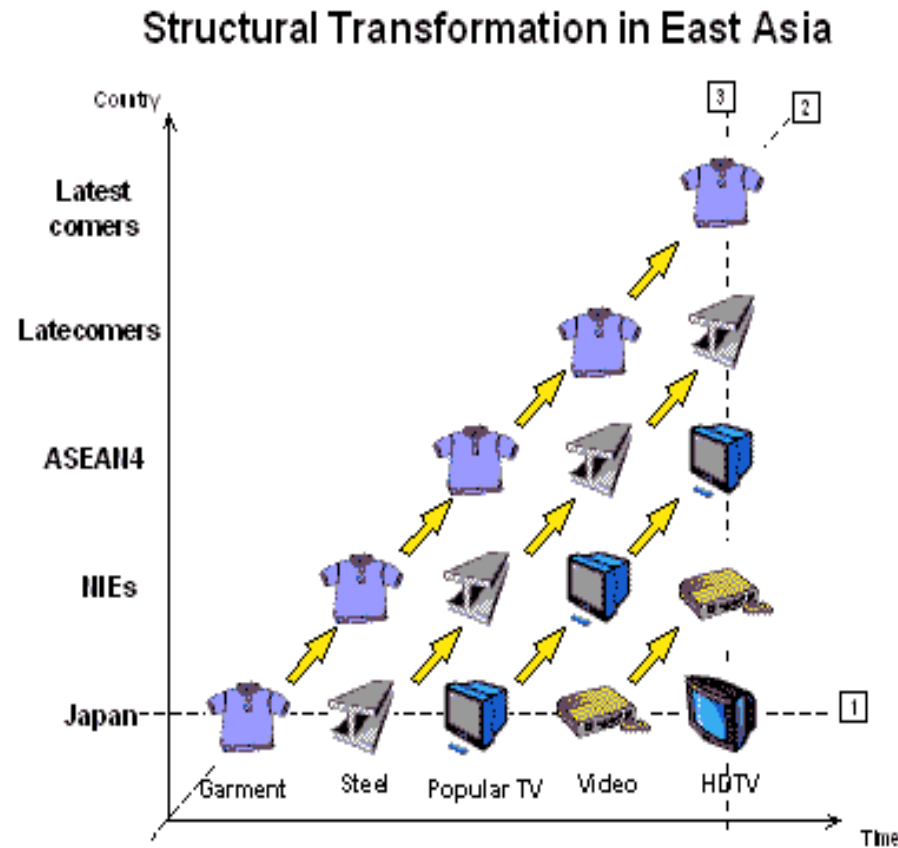
Step 6:

The government may compensate pioneer firms in the listed identified above with

- Tax incentives for a limited period,
- Direct credits for investments,
- Access to foreign exchanges

THE NEW OPPORTUNITIES FOR UZBEKISTAN IN THE MULTI- POLAR GROWTH WORLD

Historically, the dynamically growing developing countries achieve rapid structure transformation by tapping into the latecomer advantages in a flying-geese pattern



The New Opportunities arise from the industrial upgrading of China and other new growth poles

	year	GDP per capita, constant USD		Manufacturing		
		2000 USD	2005 USD, PPP	as % of Total Value Added	as % of Labor	employment in millions
China	2009	2206	6200	43%	17.7**	85
Japan	1960	5493	6976	35%	20**	9.7**
S.Korea	1982	3709	6123	25%	14.6	2.3
**In 1963						
*In 2002						

- Japan's industrial upgrading in the 1960s provided the opportunity for East Asia Tigers' industrial upgrading and dynamic growth
- The East Asian Tigers' industrial upgrading in the 1980s provided a similar opportunity for China.
- Now China and other new growth poles such as Brazil and India have reached a similar stage as Japan in the 1960s and East Asian Tigers in the 1980s. The opportunity to the developing countries will be many times of that provided by Japan and East Asian Tigers
- If Uzbekistan can use the growth identification and facilitation framework to capture this new opportunity, Uzbekistan will become one of the most dynamic economy in the world.

Two additional points

- Agricultural development is crucial for developing countries:
 - For poverty reduction, and
 - For providing capital and a market for industrial products.
- A resource-abundant country's resources will be a blessing if:
 - It has a good management of resources. (E.g., some of it must be saved for future generations, and enclave rent capture avoided.)
 - It uses (part of) the wealth generated from resources to facilitate structural transformation.

Concluding Remarks

- Uzbekistan performed outstandingly in its transition to a market economy and the recent global financial crisis
- Uzbekistan's economic performance can be further improved by facilitating industrial upgrading and diversification according to the changes in its comparative advantages and tapping into the latecomer advantages
- The government can use the Growth Identification and Facilitation framework to design industrial policy for promoting structural transformation
- The industrial upgrading of new global poles such as China, India, Brazil of other emerging market economies provide a golden opportunity for Uzbekistan to achieve a dynamic growth
- The World Bank will be happy to be a partner of Uzbekistan's success