

Good Governance

Influence of the government on development

Kom verder. Saxion.

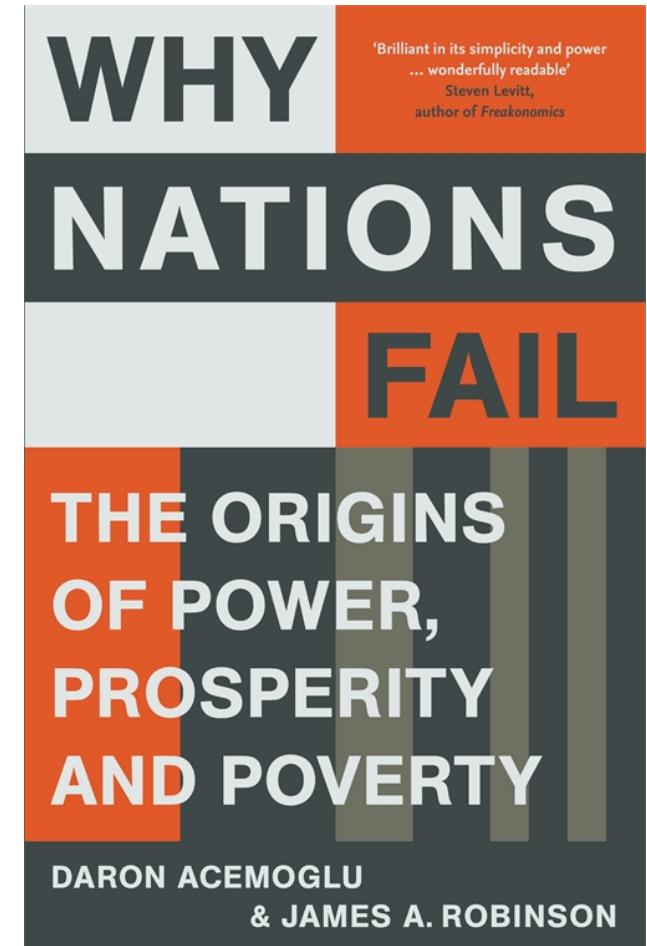
Jacques Bazen
Lecturer International Economic Relations



Outline

- The necessity of a good government for development
- Factors influencing the quality of a government
- Thoughts about development

The Good, the Bad and the Ugly: The consequences of poor government performance



Papua New Guinea – Big Men of the Wantok

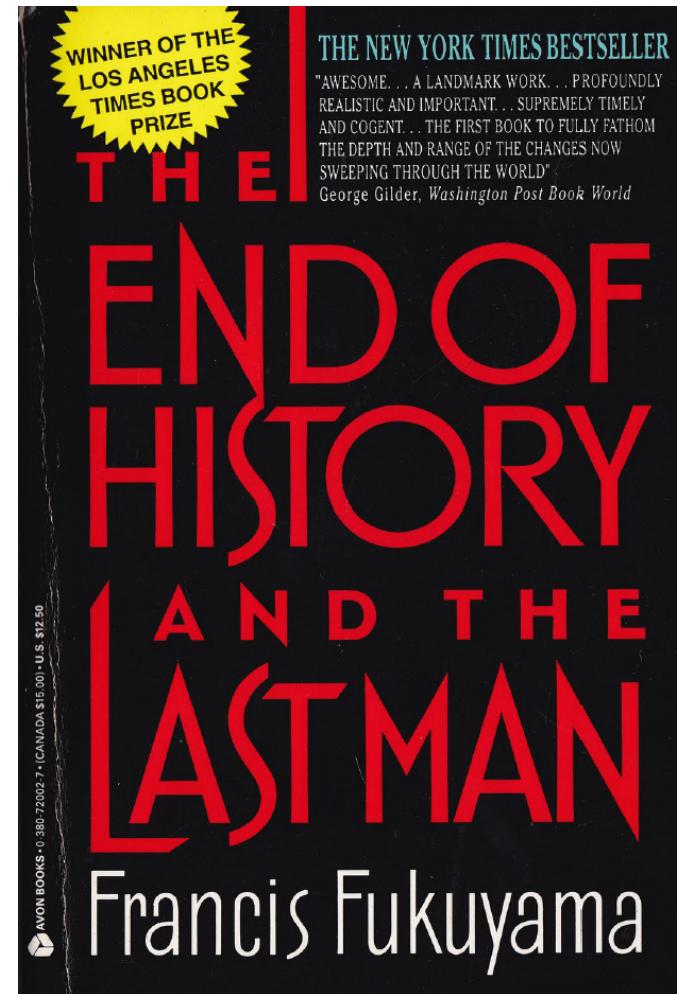


Thinking about our society

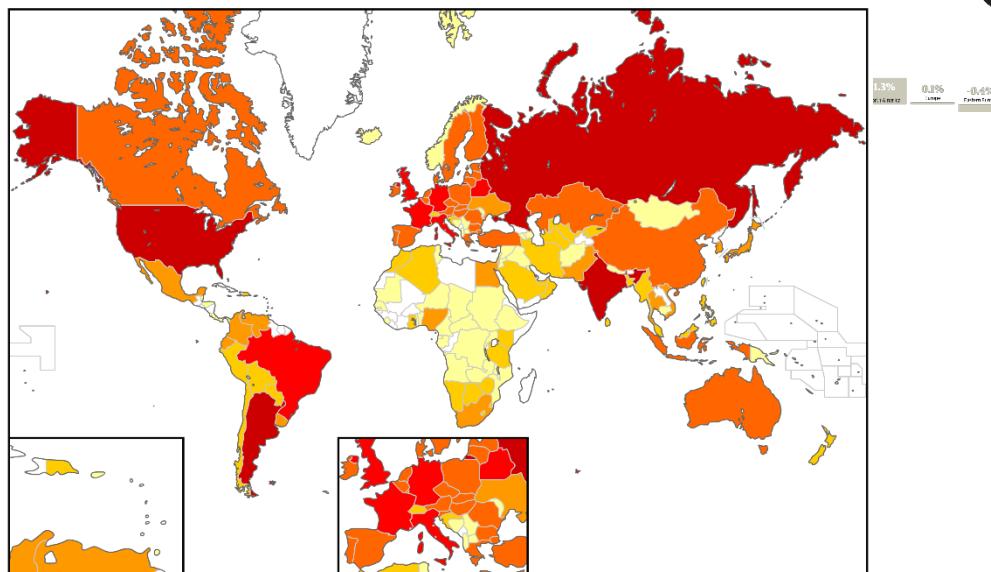
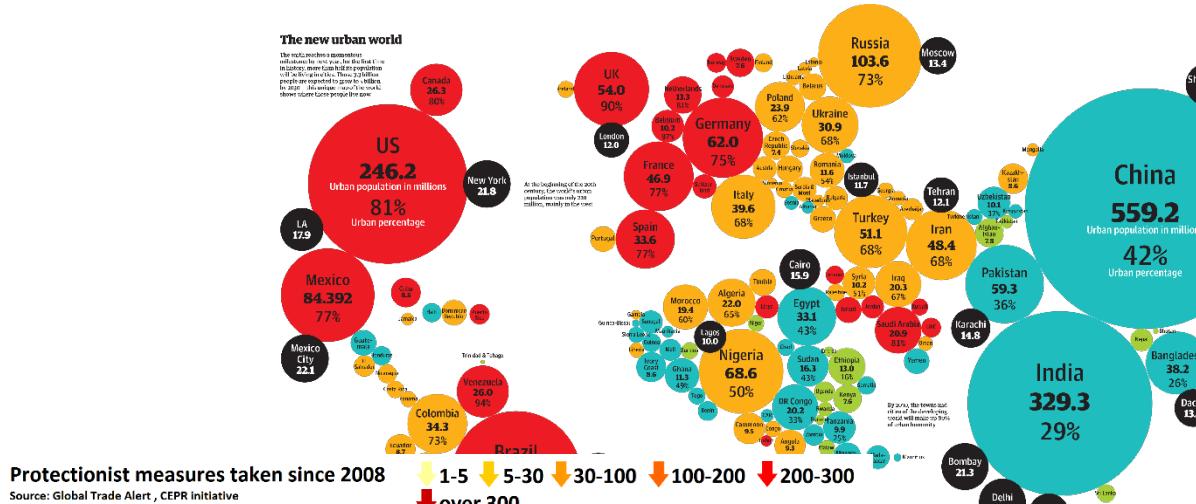
Fukuyama, 1989:

The end of History (with capital H), since it appears that capitalism from now on will be the only model, as competing systems have been taken out.

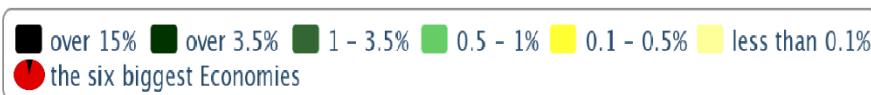
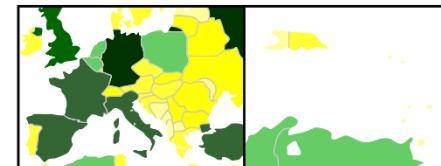
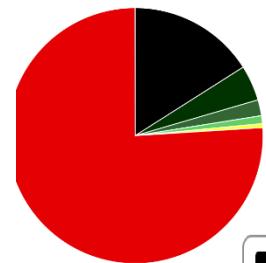
Capitalism involves the free market exchange of goods, worldwide → development of more and more global trading



What does the world economy look like?



3,307,950,000
The world's urban population – from a total of 6,615.9 million

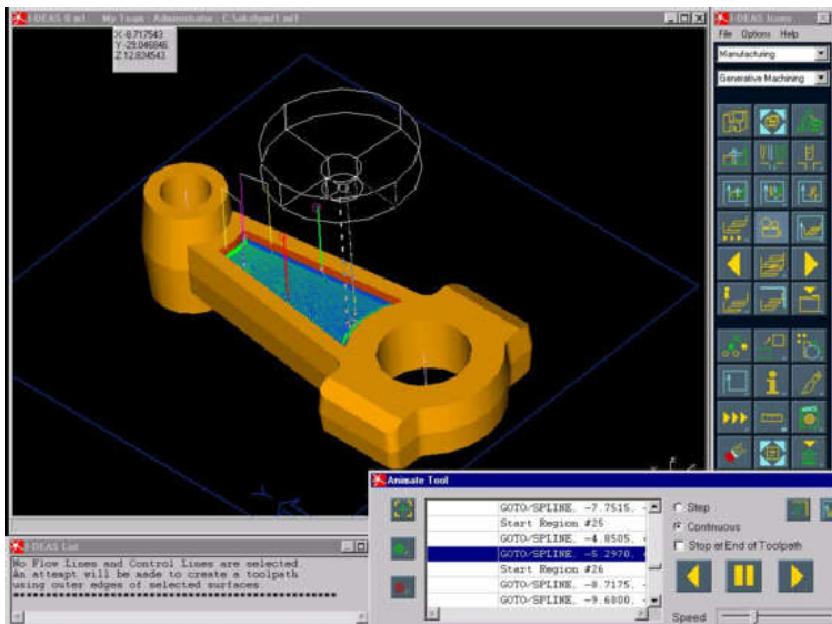


Share of World GDP PPP 2011, World Bank, ICP

What trends and Developments can be observed?

In the present day globalized world, regions and countries get connected more and more because of:

- Better communication
- Cheaper and better transport



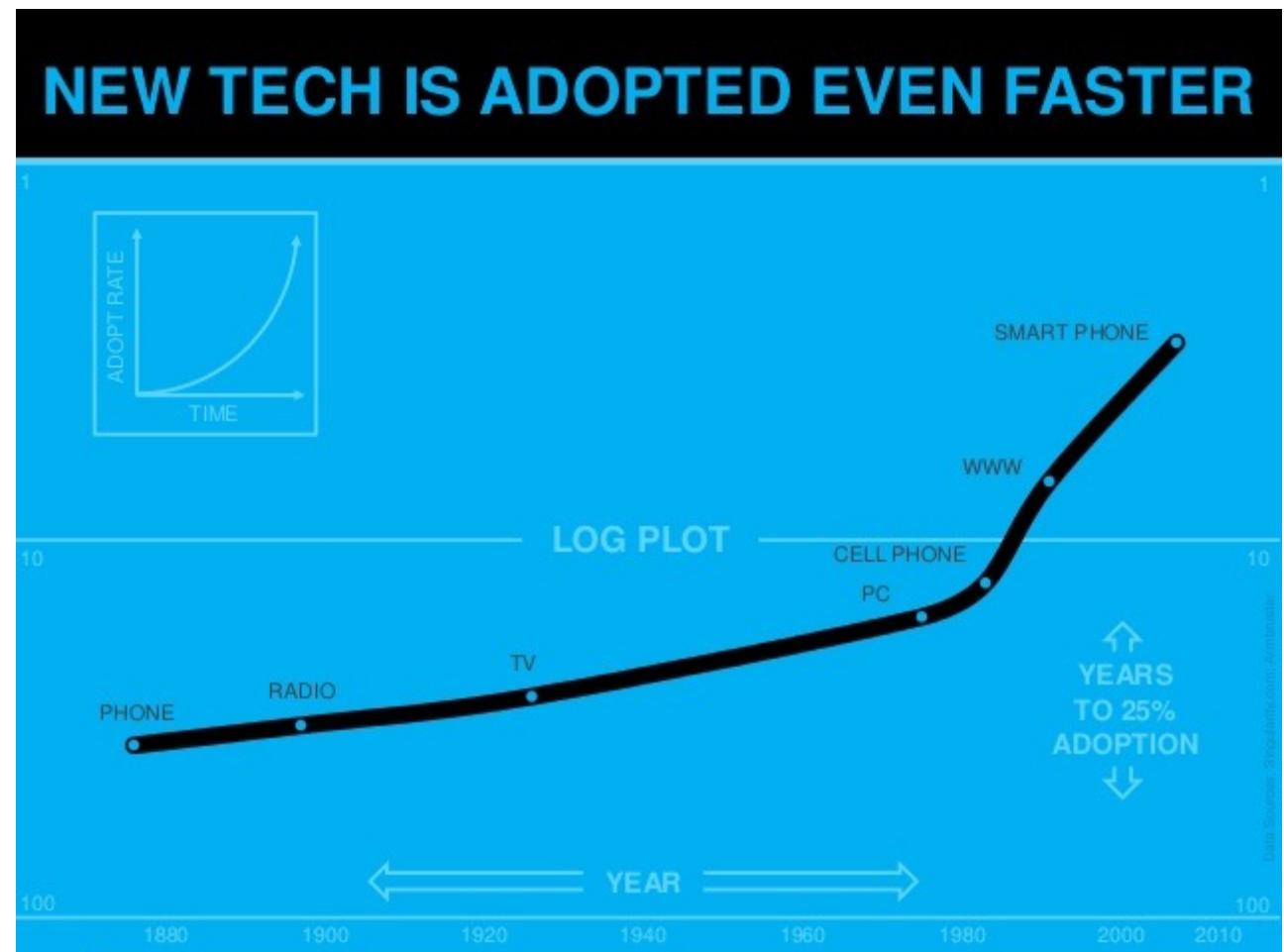
200 - 300 men
100 ton freight



13 men
14700 TEU

Exponential times

https://www.youtube.com/watch?v=uqZiLO0YI7Y&feature=iv&src_vid=XrJjfDUzD7M&annotation_id=annotation_1871640555



Some thoughts: The end of History

“Modern liberal corporate friendly capitalism is the final stage of human development. No further real competing systems can be found anywhere on the planet”.

According to Francis Fukuyama

Good for entrepreneurs?

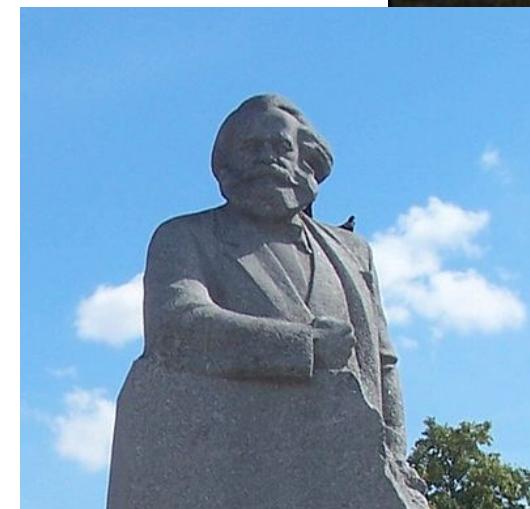


Role of entrepreneurship

“Slowly but surely, entrepreneurship will disappear, in its place will be large corporations who by means of their capital have all the power and control.” Joseph Schumpeter (Capitalism, Socialism and Democracy)

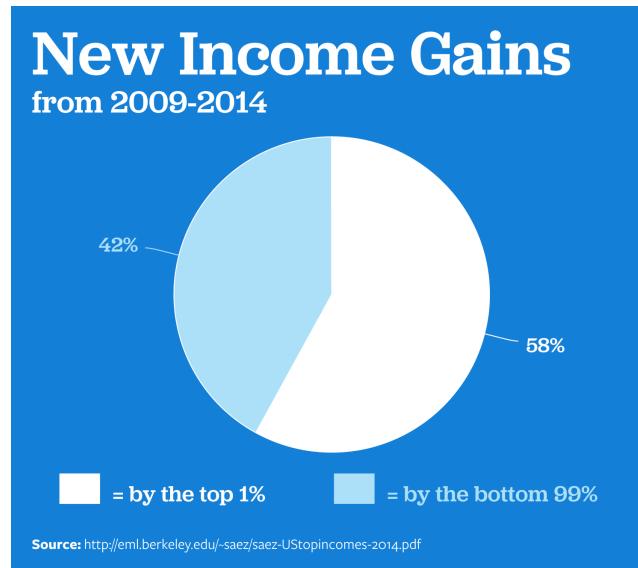


“The economic system is shaped by the accumulation of capital. There will be less and less opportunities for the common man. This will lead to a revolution”. Karl Marx

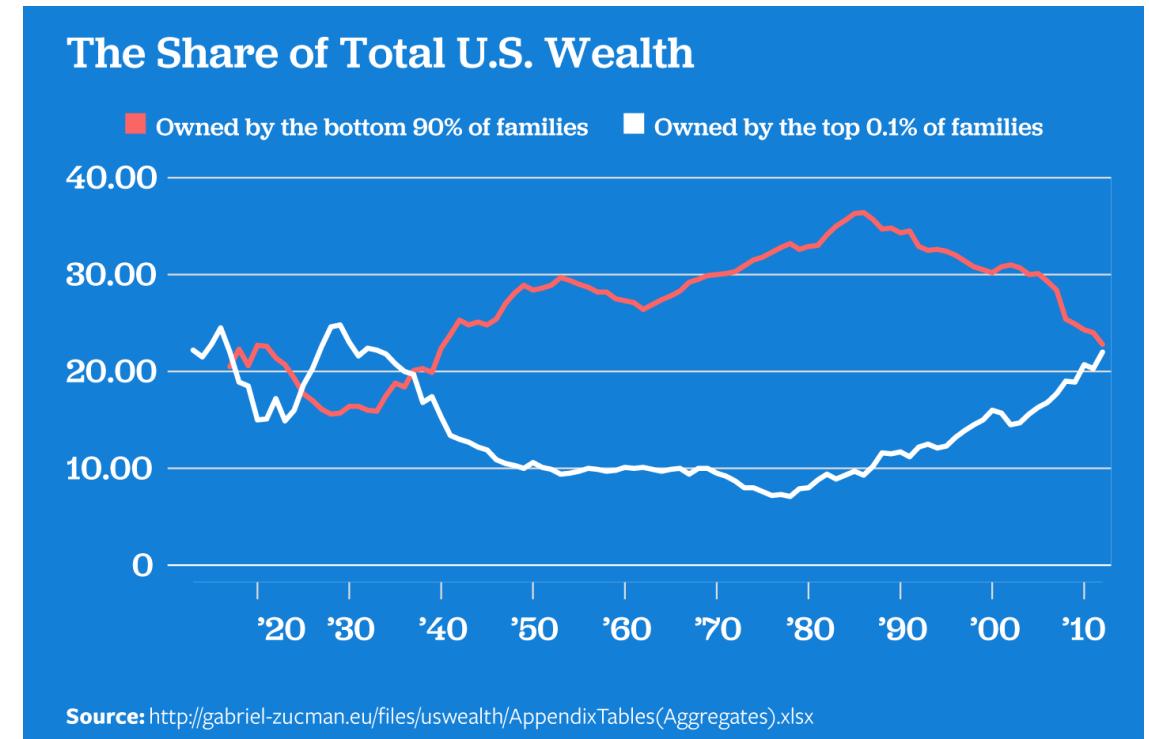


Are these trends visible?

Wealth inequality: bad for entrepreneurs?



"The three richest persons on this planet own as much as the 48 poorest nations combined", OECD 2011



Entrepreneurs as seekers of niche markets

Friedrich Von Hayek: “*Out of seemingly chaos, economic order and structure will appear automatically, driven by market forces*”.

Entrepreneurs are perfect in spotting and using “market imperfections”

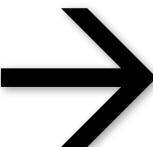


Role of Entrepreneurs

The role of entrepreneurs is those of the so-called: “*Free spirits*”, who initiate innovation and creative destruction (new replaces old). According to Schumpeter.



Spotify®



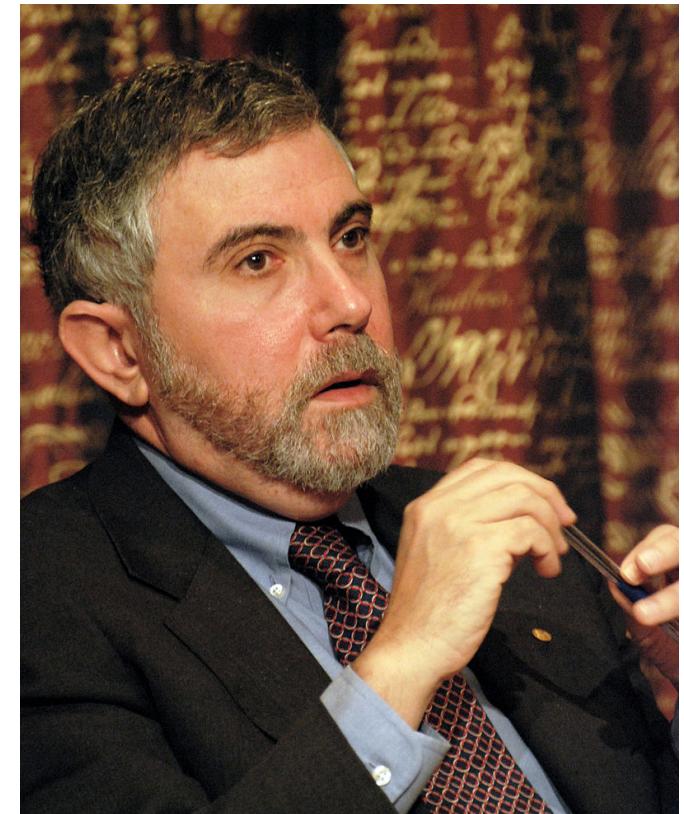
?

Technology causes Economic Growth

Paul Krugman, new growth theory:
Through *technology* economies can truly grow.

Real economic development is only possible with technological development.

So... we need tech entrepreneurs only?



Developments in society

Current *long-term* trends and development

- Globalization and trade liberalization
- Development of Asia



Pre-Modern Economics

In the 17th and 18th century, European nations adopted “Mercantilist” policies.

- Trade is zero-sum. One wins, the other loses
- Fixed amount of money
- Protectionism, subsidizing export, taxing import
- Frequent trade wars

Trade wars

"De Ruyter burning the English fleet at Chatham",
by Peter van der Velde



Mercantilism

Mercantilism was a reaction on the city-based trade of the Middle Ages



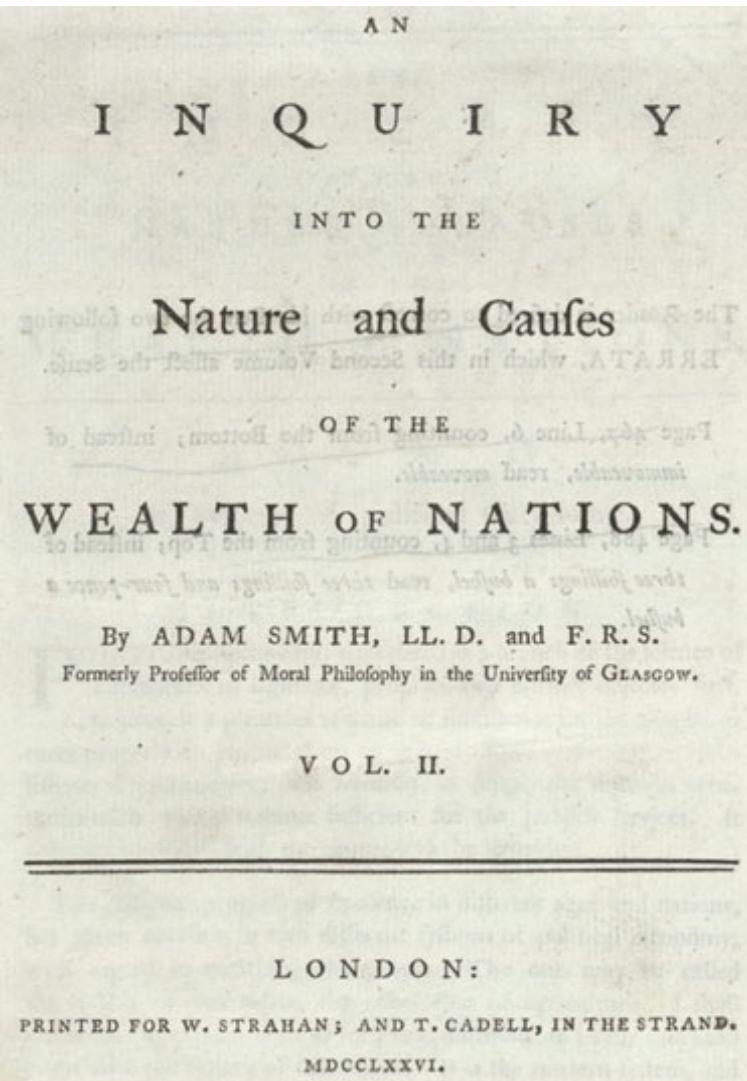
Can you give an aspect of mercantilism?

Birth of the modern economy: Adam Smith

During the 18th century more and more criticism on the Mercantilist model.

Most important book: Adam Smith with his book “*An Inquiry into the Nature and Causes of the Wealth of Nations*”

Adam Smith



Wealth of Nations

Criticism on Mercantilism:

1. Protectionism is not always good
2. Large amounts of gold are not required for economic prosperity

And the new idea about wealth:

“The invisible hand of the market”, people contributing to it, without even knowing.

Invisible hand of the market

What does the “Invisible hand” mean?

- Example of grain prices and government intervention
- Egoism as driving force of the market?

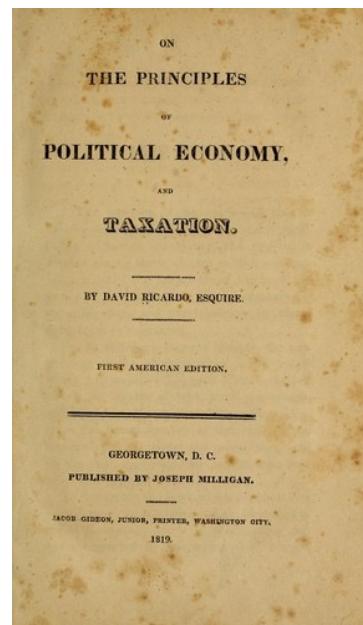
“All for ourselves, and nothing for other people, seems, in every age of the world, to have been the vile maxim of the masters of mankind”

Adam Smith and Free Trade

- Free trade is one of the factors in the “invisible hand of the market”
- Free trade leads to increased competition → cutting costs
- Free trade leads to specialization → division of labour to the areas where it is most profitable

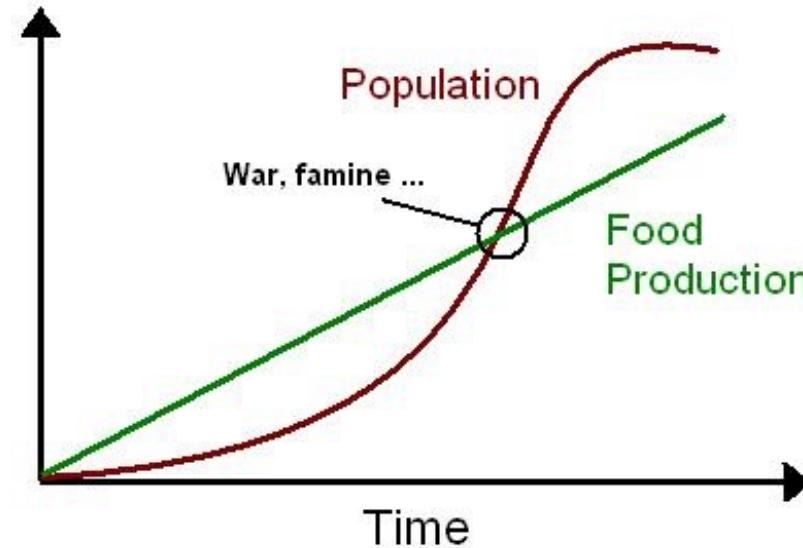
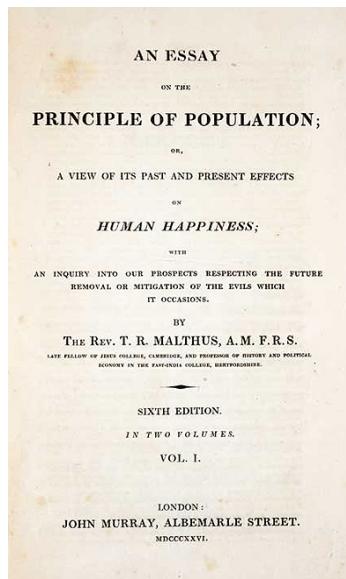
David Ricardo and Free Trade

Ricardo proved mathematically that free trade and the focus on comparative cost advantages leads to increased welfare.



World's population

Thomas Malthus: It's not Free Trade...it's the world's population that is the problem for reaching a happy wealthy society.



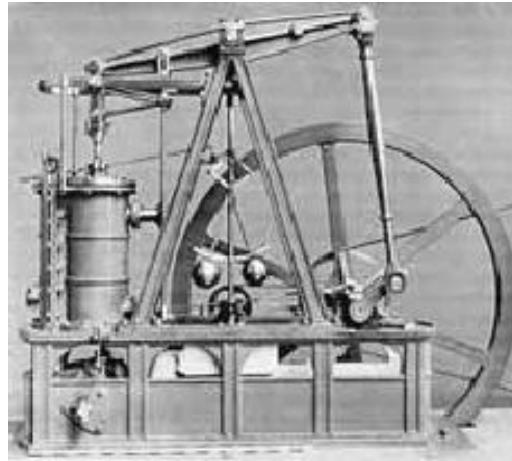




Industrial revolution

Before the Industrial Revolution: Most people worked in agriculture. The more land the better.

After the Industrial Revolution: Need for secure access to raw materials: just land surface doesn't matter anymore



Industrial revolution caused a tremendous advantage to innovative societies

- Innovation is fuelled by stability and good quality government.
- Since the industrial revolution, investments became much larger and the needs for solid property rights became even more stronger



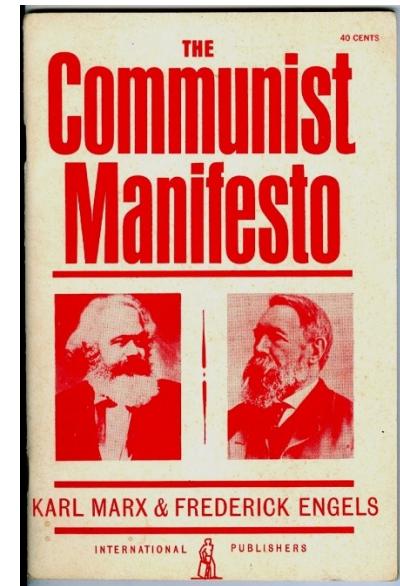
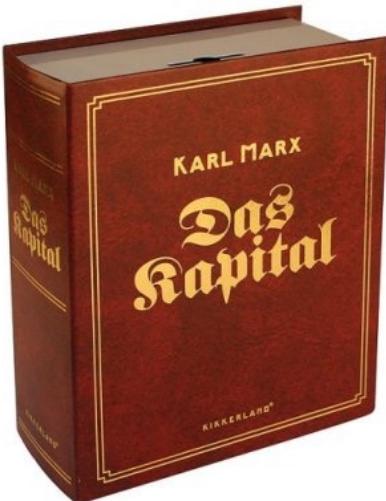
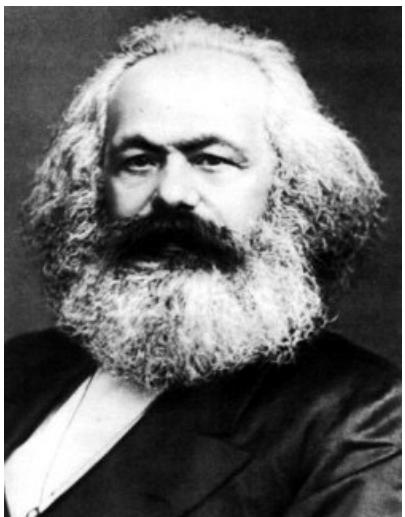
The rise of the working class

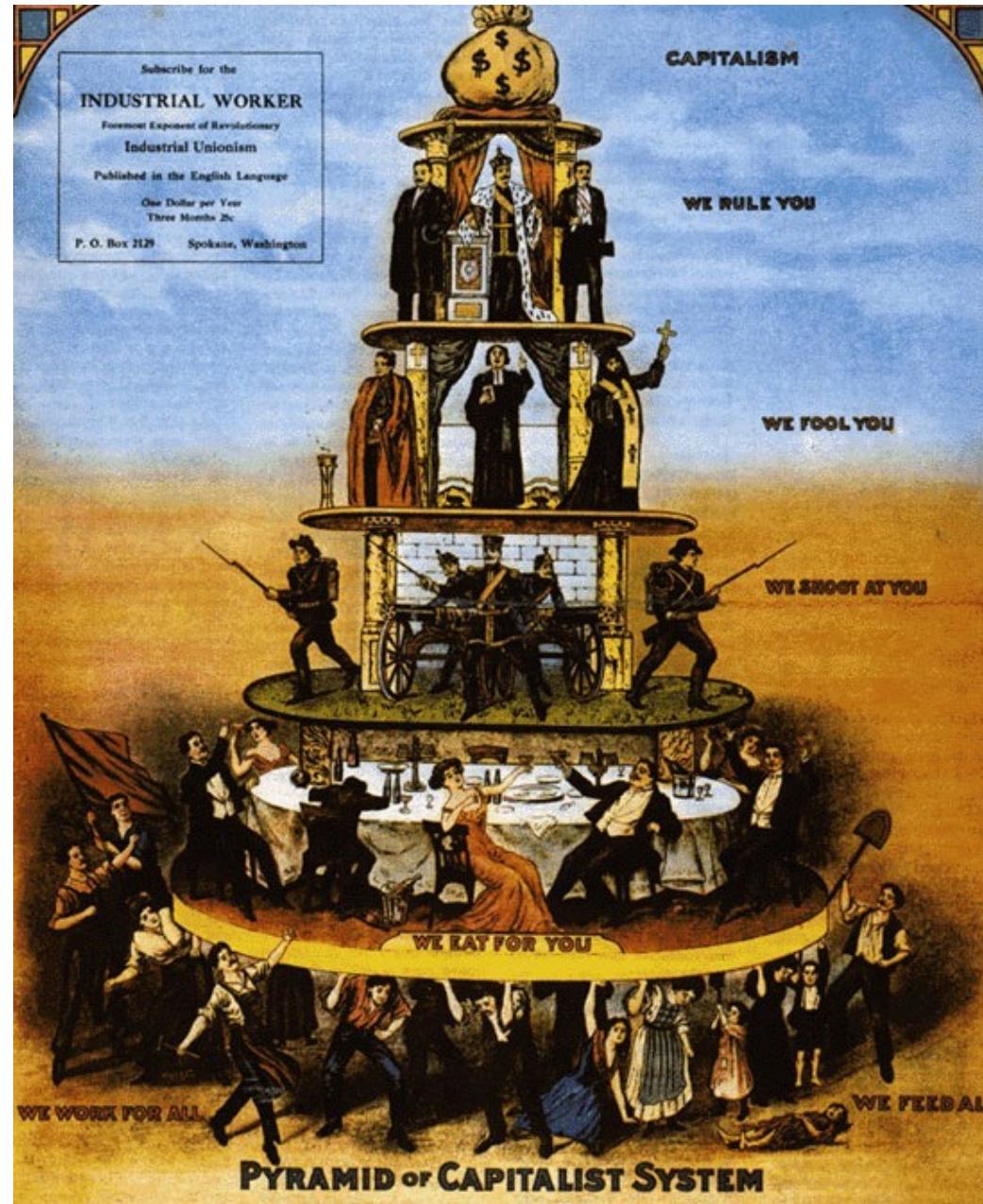
The industrial revolution changed the life of the people greatly. No longer the majority worked in agriculture, but in factories instead.

The bad, unhealthy working conditions and the low payment led to unrest and some utopian vision of the future...

The rise of the working class

Karl Marx: the current condition is not sustainable, workers in factories will unite and rebel against their exploiters: class struggle



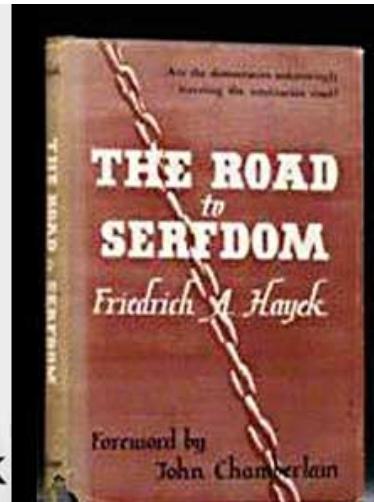


Austrian school of free market

Influential thinkers in economic history (even today) are the economists of the so-called Austrian school. Especially Friedrich Von Hayek.

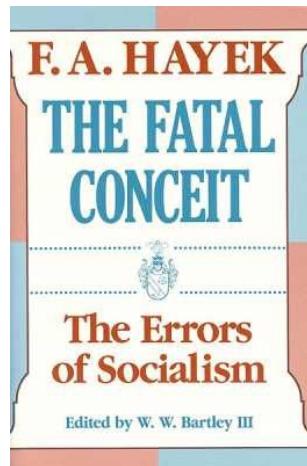


"THERE IS ALL THE
DIFFERENCE IN THE
WORLD BETWEEN
**TREATING PEOPLE
EQUALLY**
AND ATTEMPTING TO
**MAKE THEM
EQUAL**"
-F.A. HAYEK



Birth of civilization (Hayek)

The right for private property is the birth of civilization: solid private property rights make people invest and use their property. The language they use: the price mechanism.



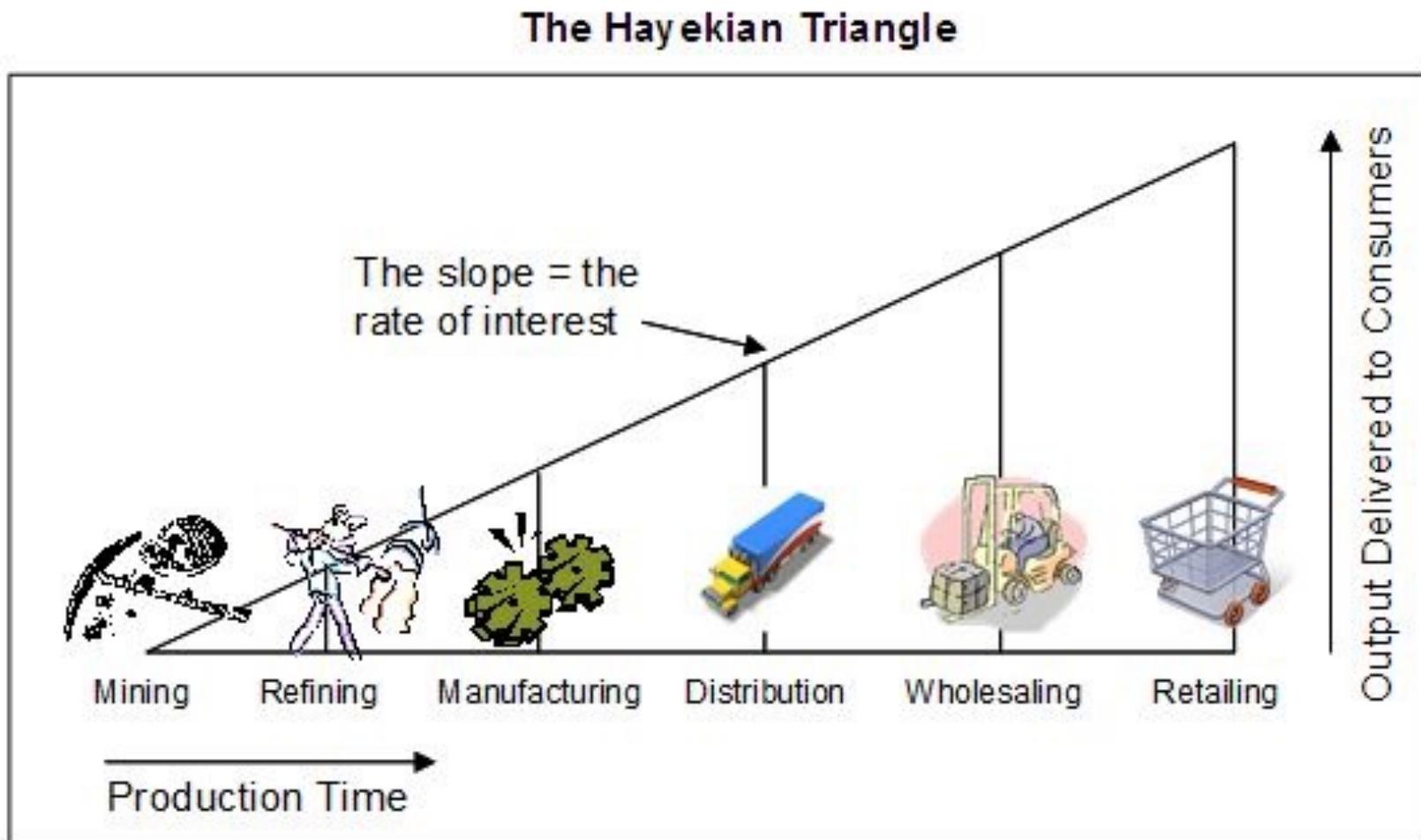
"To the naive mind that can conceive of order only as the product of deliberate arrangement, it may seem absurd that in complex conditions order, and adaptation to the unknown, can be achieved more effectively by decentralizing decisions and that a division of authority will actually extend the possibility of overall order. Yet that decentralization actually leads to more information being taken into account."

F.A. Hayek

@CPSThinkTank



Boom – Bust cycles



Attention for the demand side

Most economists looked especially into the supply side of the economy.

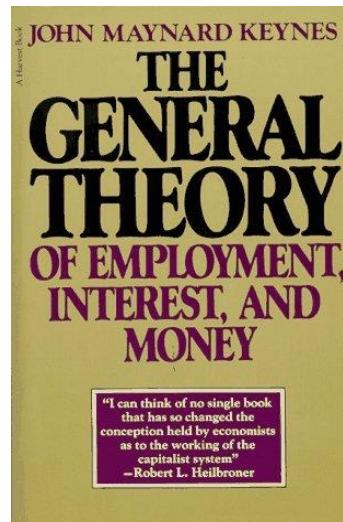
For example Adam Smith: If there is scarcity of a certain good, then the price goes up. That stimulates production, so that the supply of that good will grow again.

Attention for the demand side

Actually...maybe the production can also be stimulated if the demand goes up...

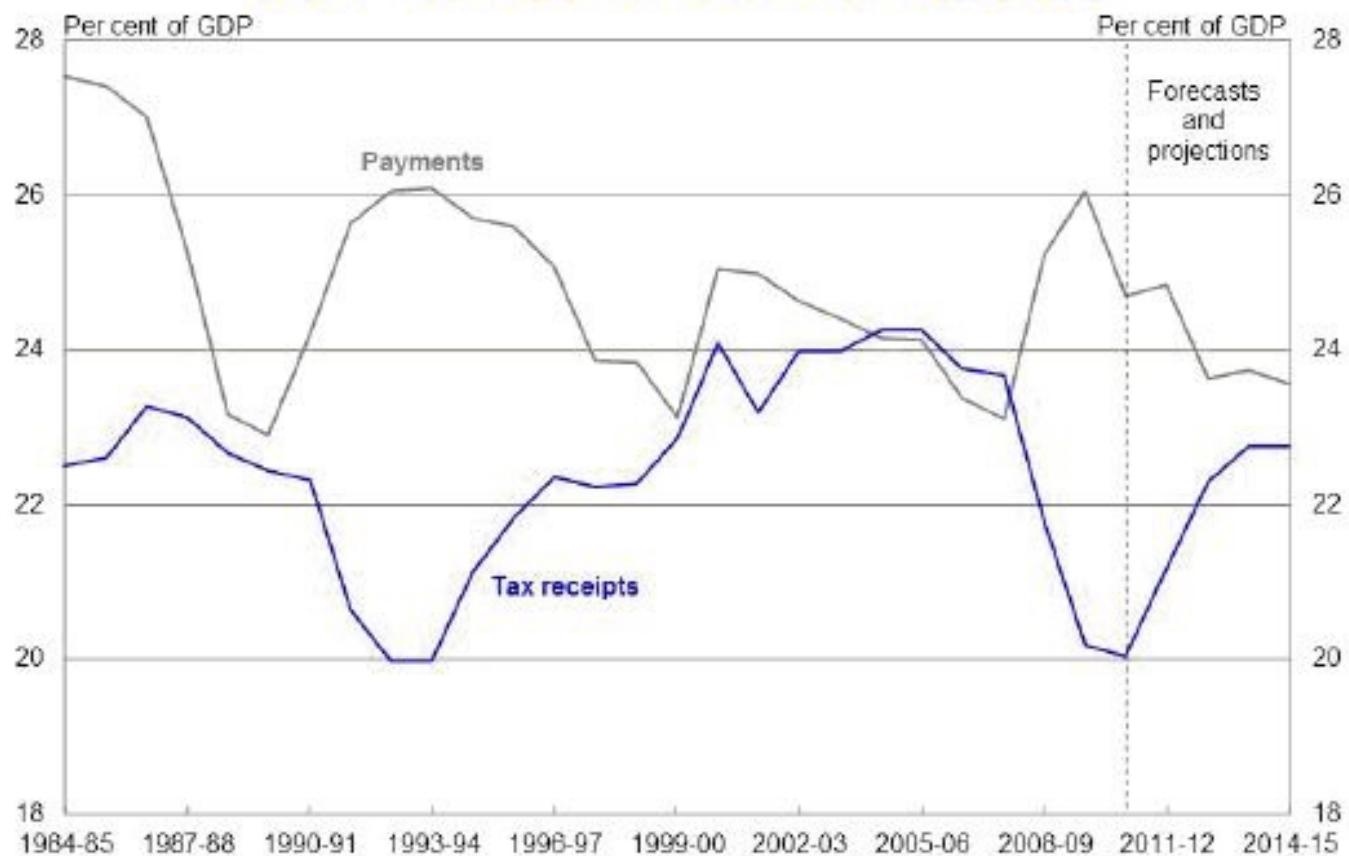
John Maynard Keynes:

General Theory of Employment, Interest and Money



Demand side: Countercyclical policy

Tax receipts and total payments to GDP since the mid-1980s



The big economic debate

Hayek vs. Keynes
(free market vs. government spending)

- <http://www.youtube.com/watch?v=d0nERTFo-Sk>
- http://www.youtube.com/watch?v=BUmDxbMwN_Y



Keynes vs. Hayek?

In reality... Unless followed to the extreme, Keynes and Hayek do actually offer a complementary approach to economic recovery.

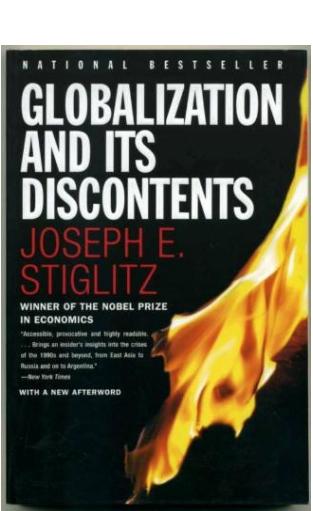
Keynes vs. Hayek?

Keynes was never a fan of continued government spending (*only for kick-starting the economy*)

Hayek was never a fan of complete laissez-faire capitalism: “*In no system that could be rationally defended would the state just do nothing. Instead it would take care of the weakest*”

Attention for the role of power

Economists often assume a free market with perfect information exist. Joseph Stiglitz suggests this is not the case: Asymmetrical markets.

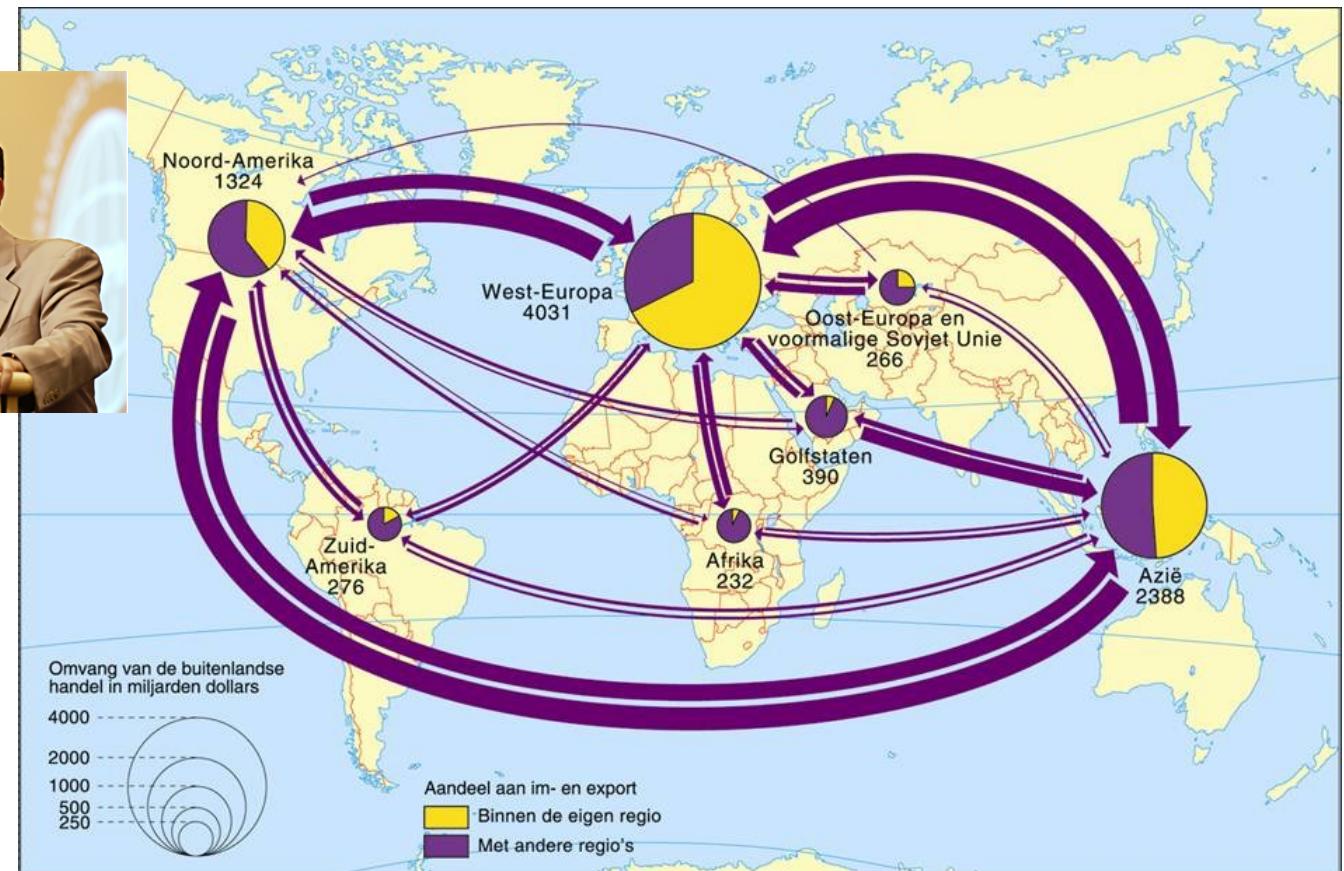
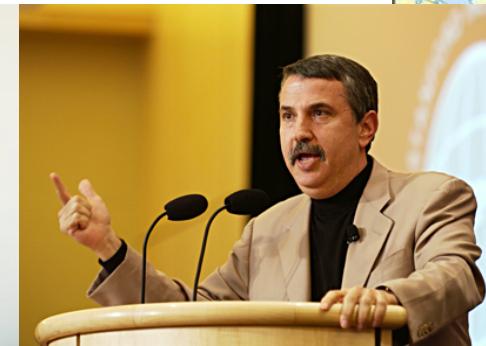
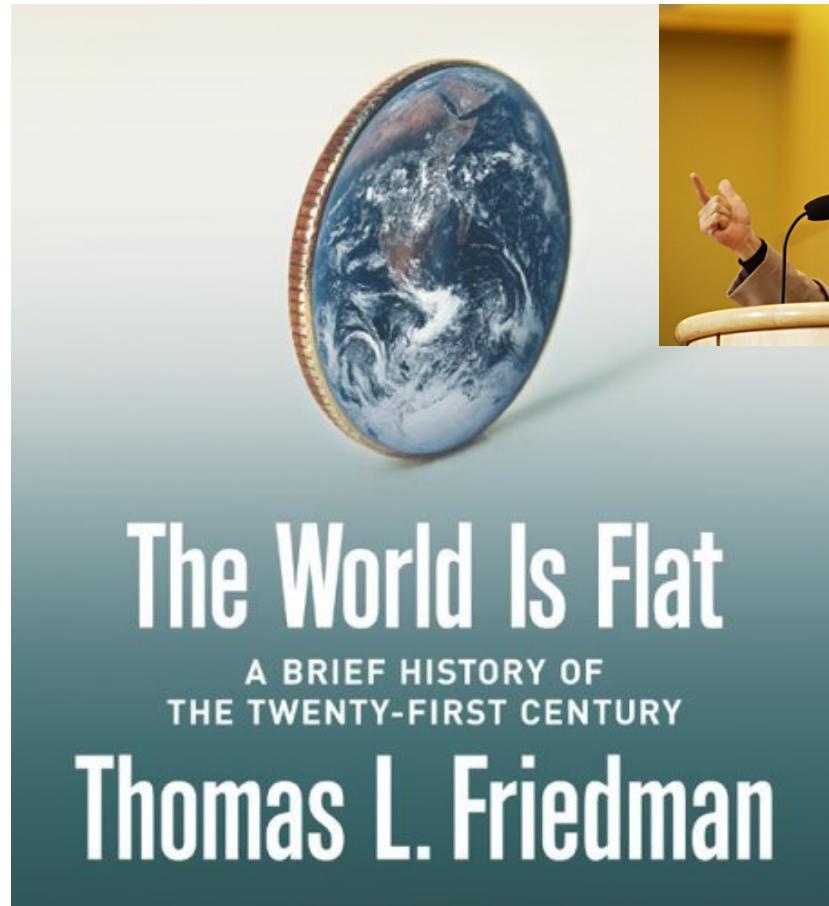


"The top 1 per cent have the best houses, the best educations, the best doctors, and the best lifestyles, but there is one thing that money doesn't seem to have bought: an understanding that their fate is bound up with how the other 99 per cent live. Throughout history, this is something that the top 1 per cent eventually do learn. Too Late."

~Joseph Stiglitz

21st century Globalization: The world is flat

- The Global Village



Increased opportunities for everyone?

- Better possibilities for previously underdeveloped and peripheral countries to engage in the world economy
- Threat for employment of previously rich and developed world?
- Counteracting this threat in the west: Economic cooperation.

European cooperation

- Europe is no exception to the rule: more and more international cooperation
- Jean Monnet, cooperation to win the First World War



European cooperation

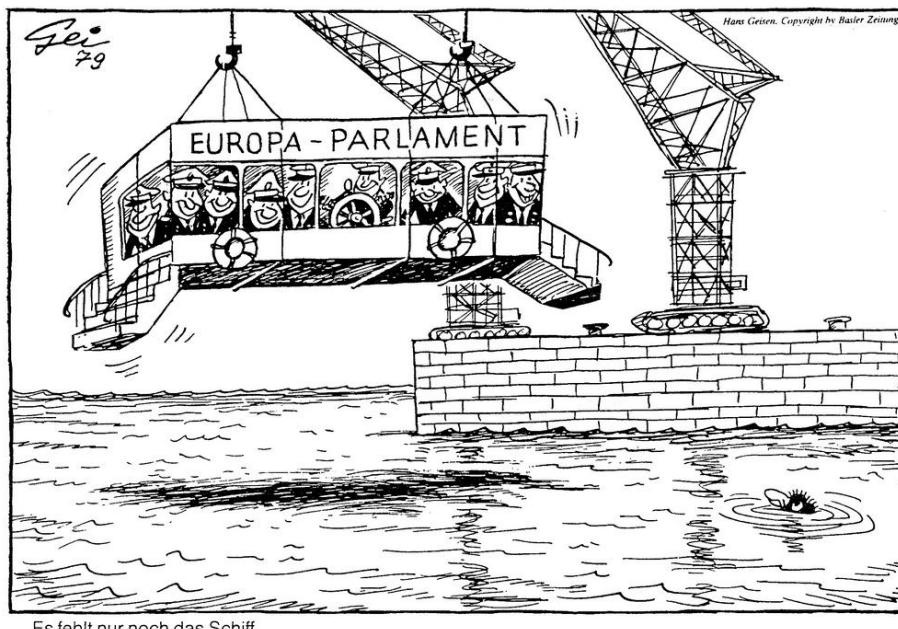
- Goal: Cooperation to ensure peace.
- Means: economic cooperation



European Union

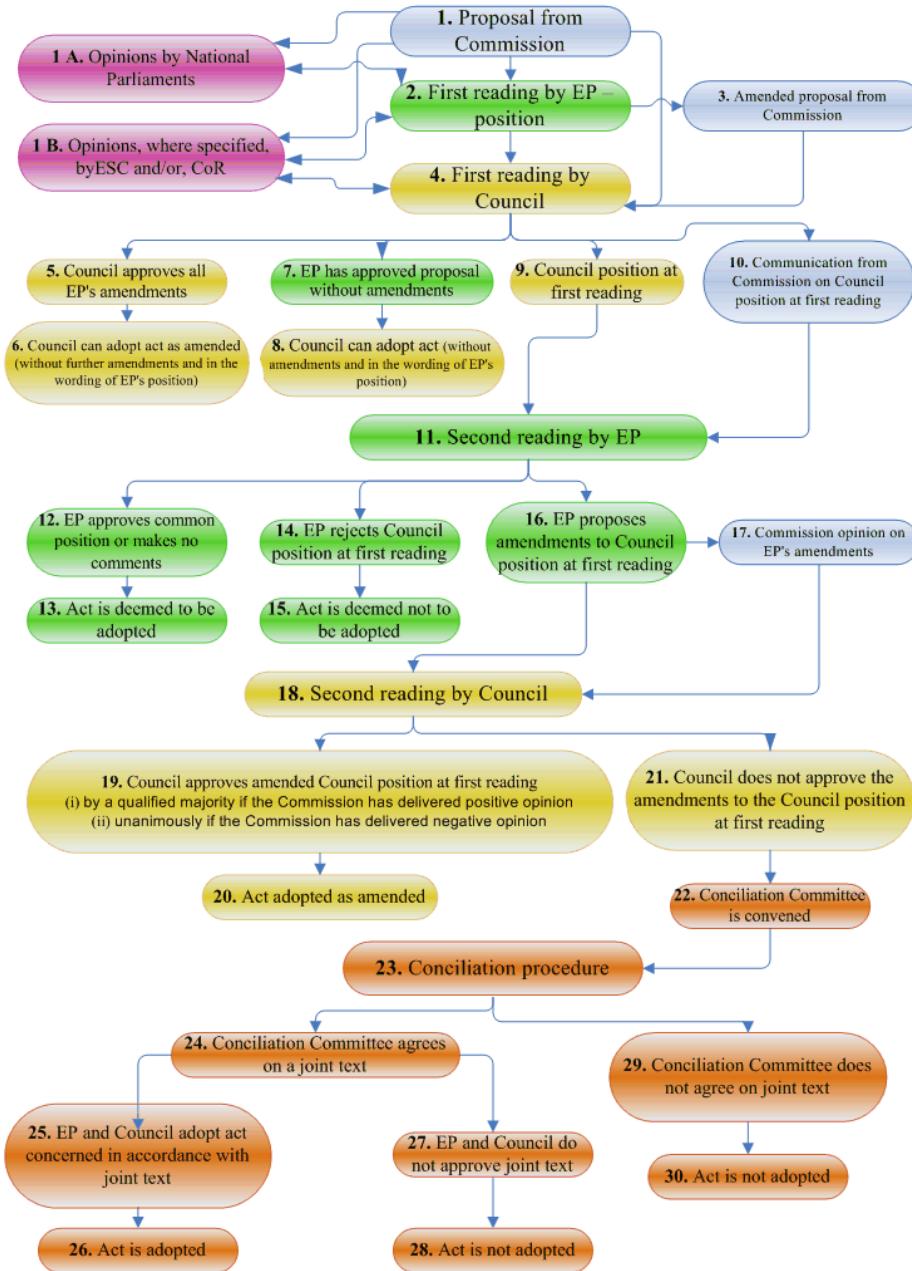
Governance model:

- Federation / Supra-National state?
- Intergovernmental cooperation?



Who is the boss of the EU?

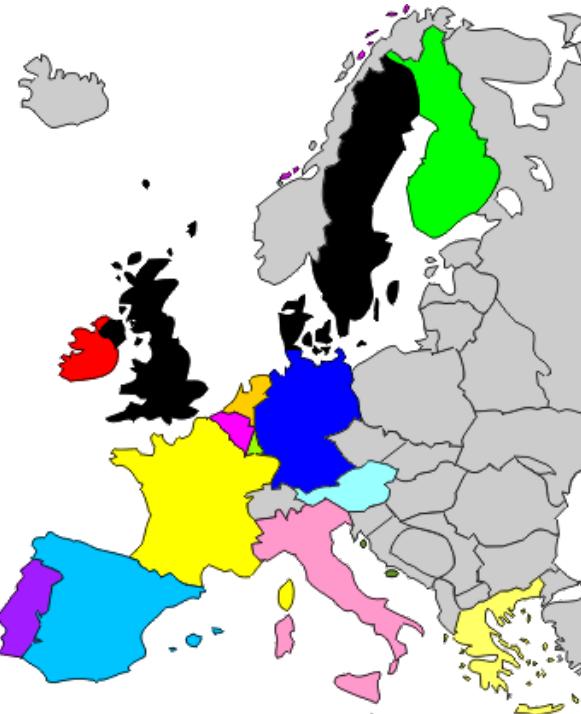




EU Decision making structure

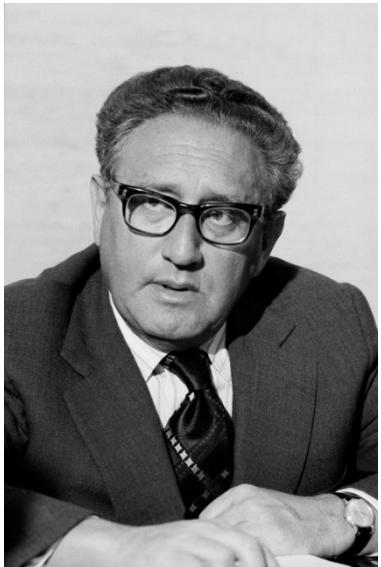
European Union

- Governance model - hybrid form
- Very complicated co-decision procedures: lack of understanding of the general population



USA

Hegemony. Desirable situation?



PROJECT FOR THE
NEW AMERICAN CENTURY



Bad Government examples

North Korea

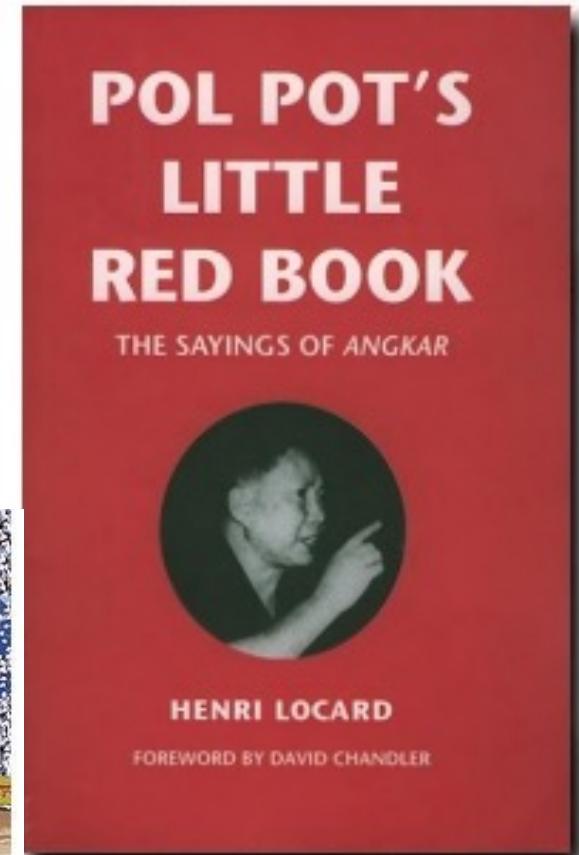
Goal: Self-sufficient agrarian-industrial state
Military spending



Bad government

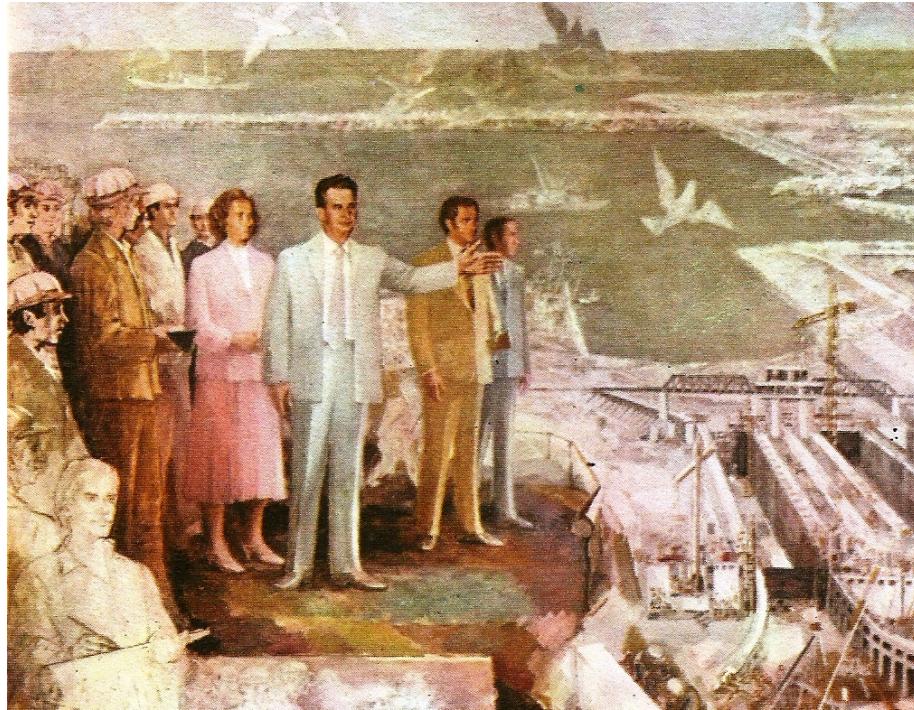
Cambodia - Khmer Rouge (Pol Pot)

Focus on getting a self-sufficient agrarian state



Isolationism - Striving for autarky

Romania (1980s)

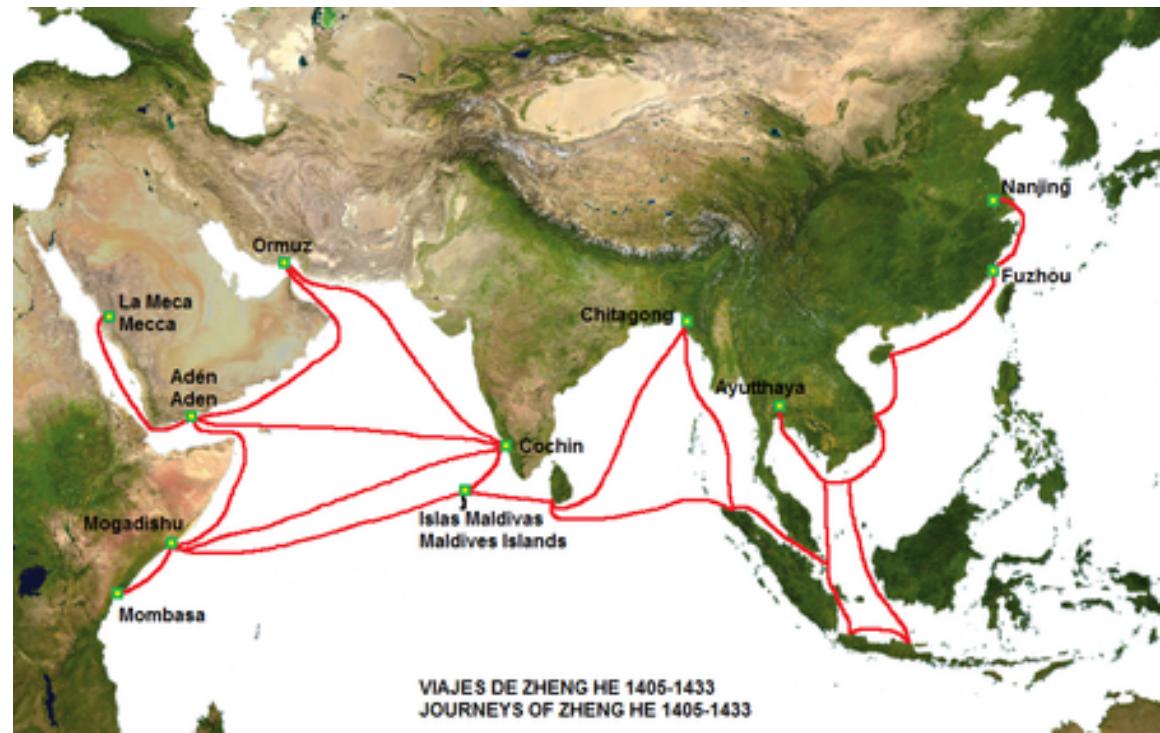


Isolationism – the case of China

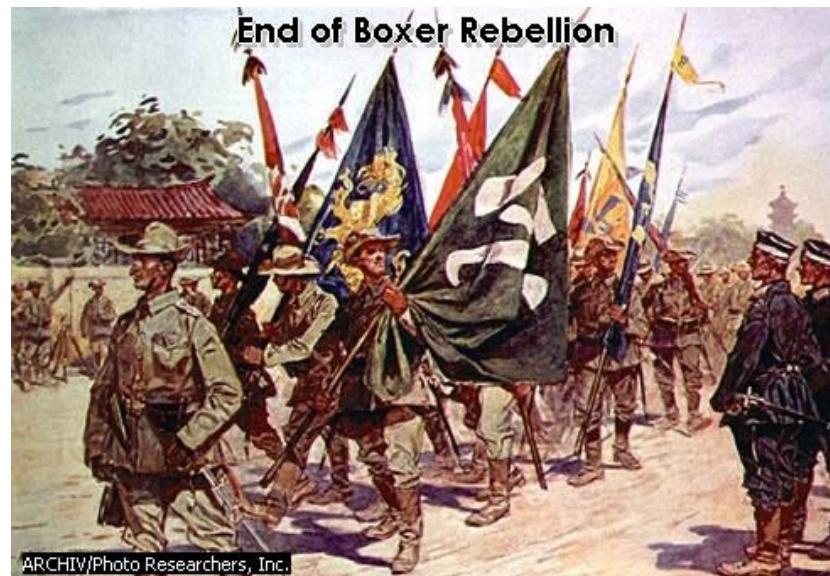
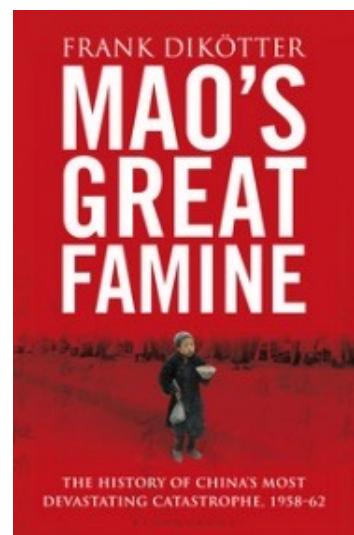


Chinese voyages of discovery

Travels of Zheng He



Eclipse of China



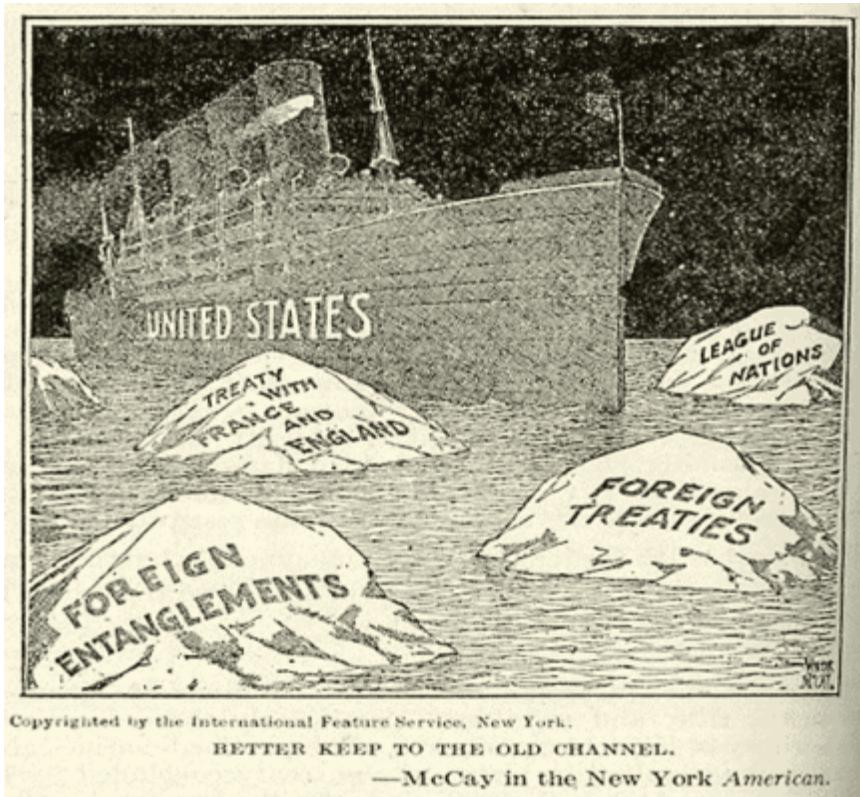
Return of China on the World Stage

Deng Xiaoping



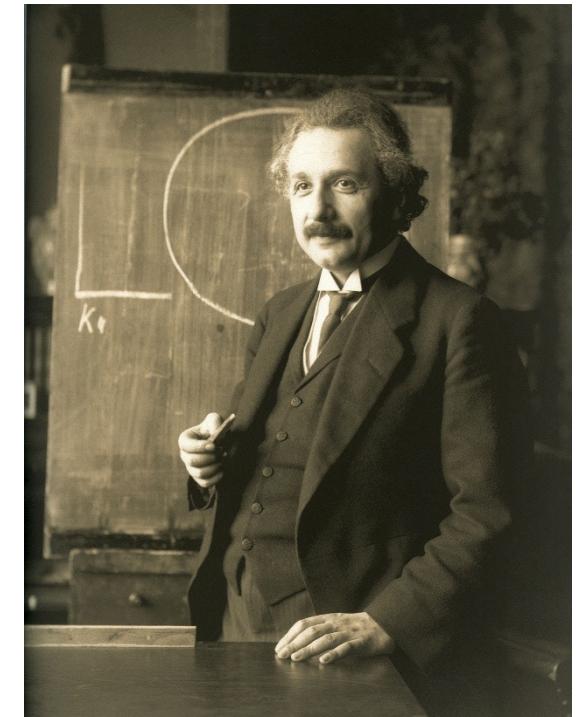
Isolationism – the case of the USA

USA in the interwar period



Difference between USA and China

- China: total isolationism on order of the Emperor
- USA, only political: Economically a lot of trade and immigration. USA attracted large numbers of the worlds top talents in this period.

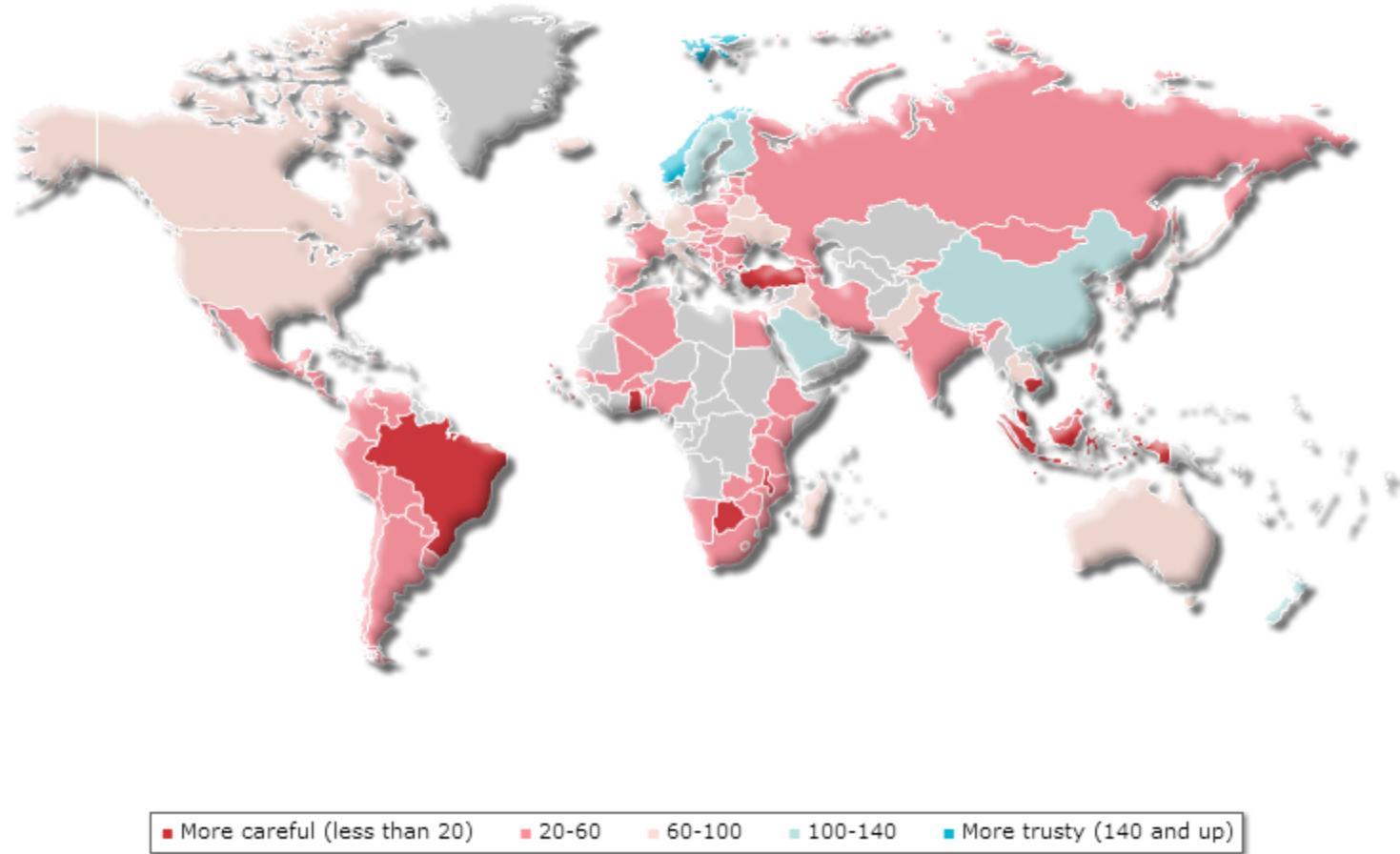


Part two: Government & Leadership

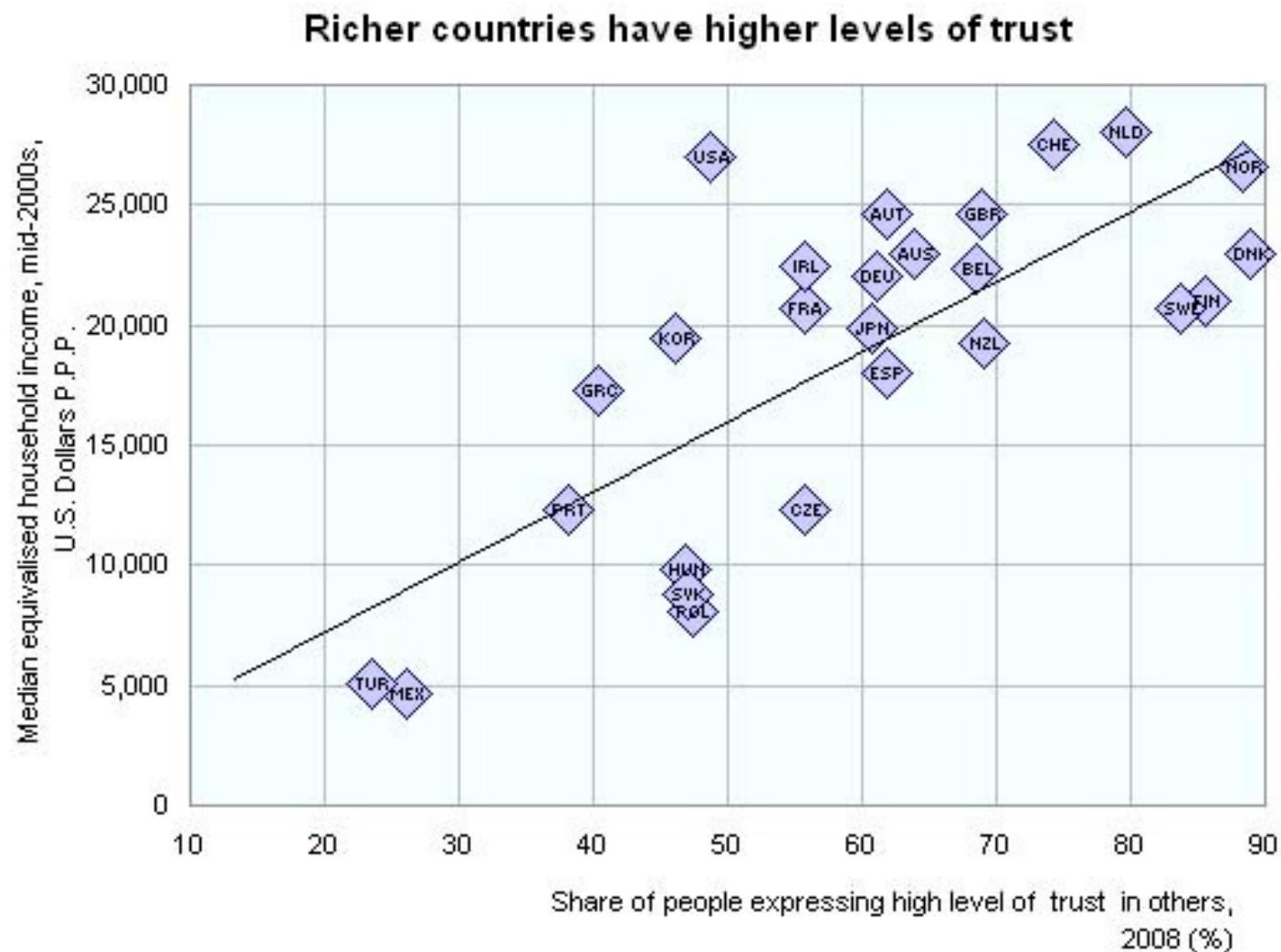


Leadership and Trust

- Trust is a consequence of good leadership
- High trust = lower transaction costs
- Trust in society, and other people leads to more investment and consequently to more economic growth

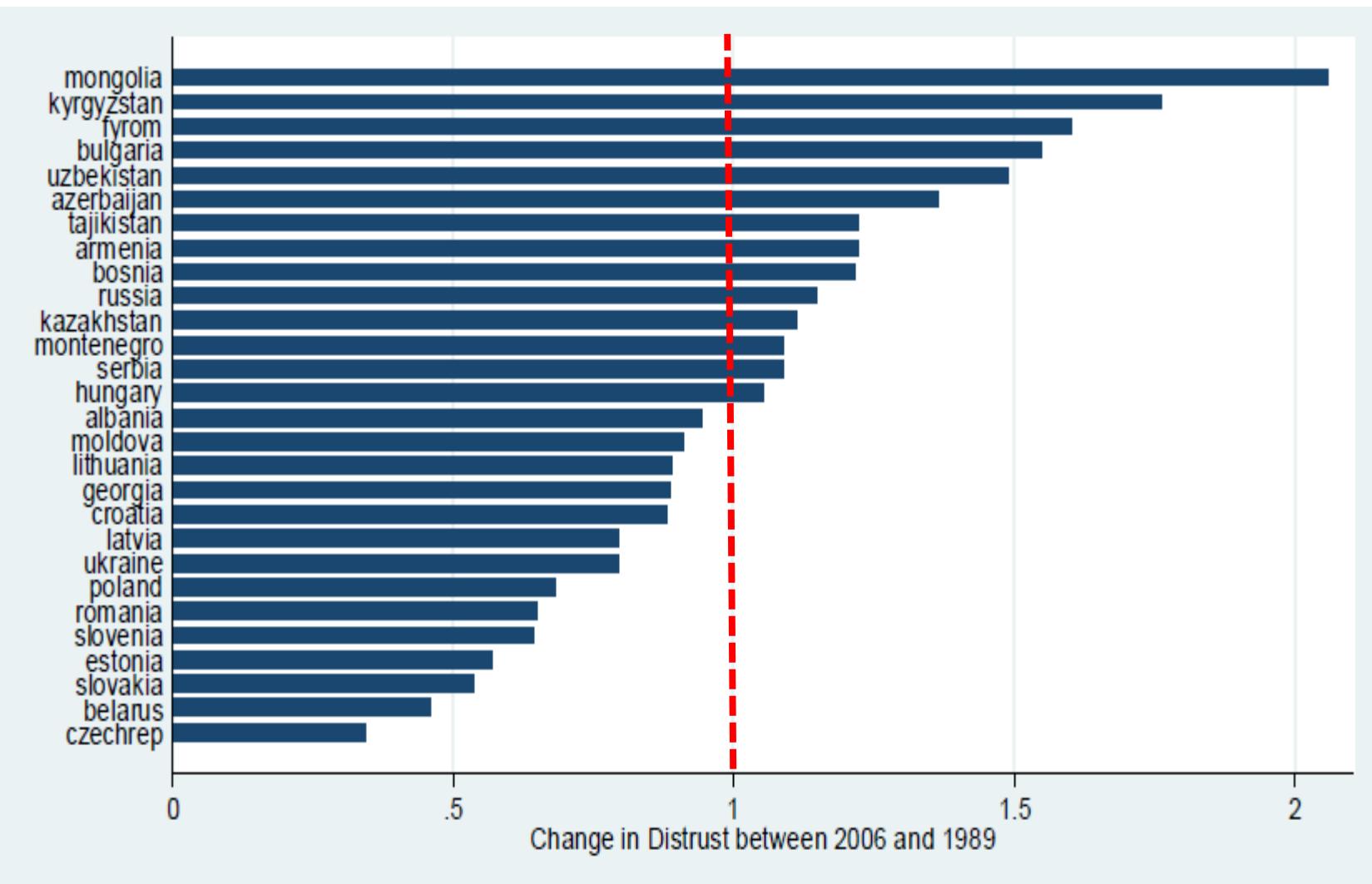


Trust & The economy



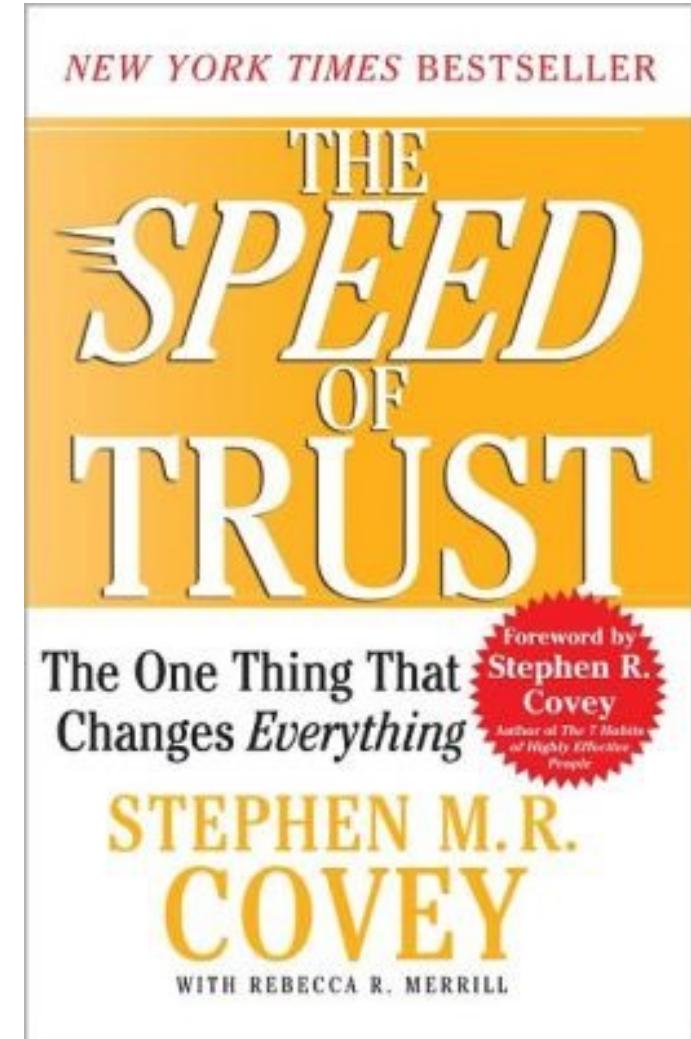
Leadership and Trust

Example of changing levels of trust in society, in former Communist countries



Why is trust so important?

- High trust lowers transaction costs in any field in society.
- Less need for expensive lawyers and complicated procedures
- More room for creative & innovative behaviour
- Faster speed of operation → lower transaction costs



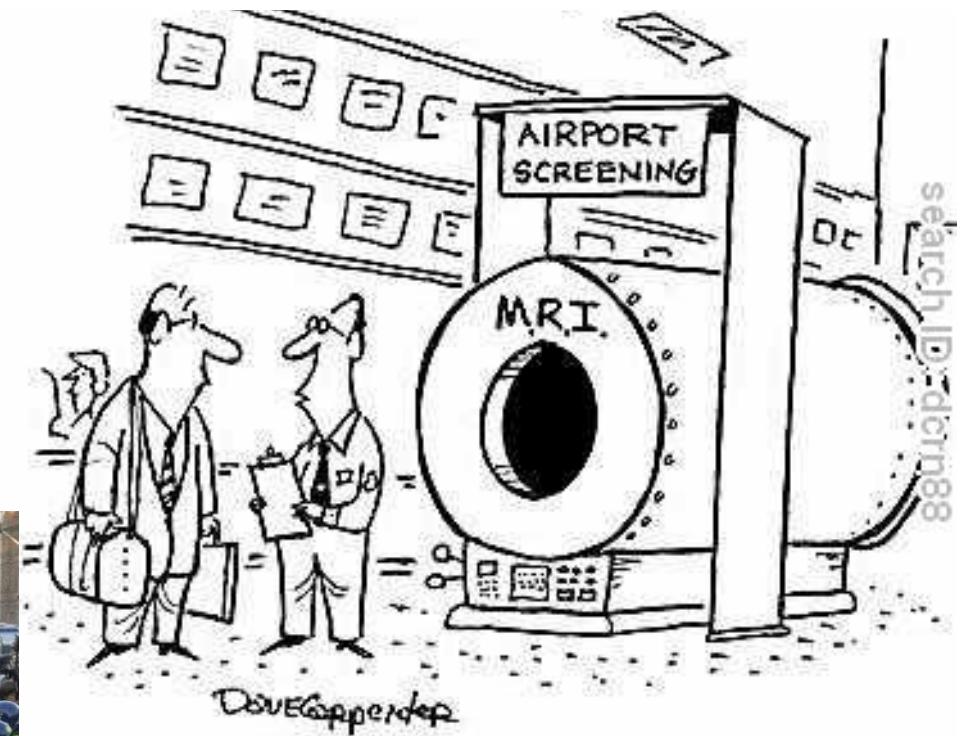
Low trust - example



Rising class of
securocrats in
European
countries



Emergence of
conspiracy theories



Airports accused of keeping
queues long so they can cash in
on £5 fast-track lanes

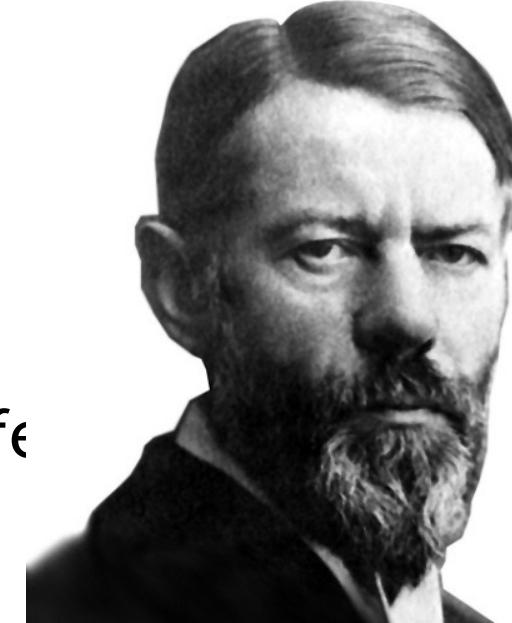
Good leadership

Crucial to organizing modern well-functioning democracies with a high wealth society is the transformation of government & politics:

- Max Weber: Development of an impersonal administration (Bureaucracy), based on meritocratic ideals.
- Fukuyama: Change of political parties from interest groups (union of ...) into programmatic parties (socialist, liberal, Christian democratic, green etc.). Not just by name, but by vision.
- Acemoglu & Robinson: Limitation to the power of the elite, checks and balances, transformation to inclusive governments
- Kjellén: Strong state, able to enforce control over its subjects.

Impersonal bureaucracy

- Specialized roles.
- Recruitment based on merit (e.g. tested through open competition).
- Uniform principles of placement, promotion, and transfer in an administrative system.
- Careerism with systematic salary structure.
- Hierarchy, responsibility and accountability.
- Subjection of official conduct to strict rules of discipline and control.
- Supremacy of abstract rules.
- Impersonal authority. (e.g. Office bearer does not bring the office with him).
- Political neutrality.



Change of political parties

In many young democracies, political parties are representing the interest of:

- Ethnic groups, clans, tribes etc.
- Religious minorities
- Patron - client related

In more mature democracies:

- Systems of thought that are interethnic, interreligious and non-patron client relation oriented.
- For example: Liberalism, Human Rights, Socialism, Christian Democracy etc.



Trust

“High trust is generally good for societies. The problem however is that when you are the only trusting person among a society of thieves and swindlers, it is not going to help you a lot...”, Francis Fukuyama.

Fukuyama: Trust and leadership can only thrive in states where institutions function. The problem is that we don't really understand how these institutions came into being and why they function as they do.

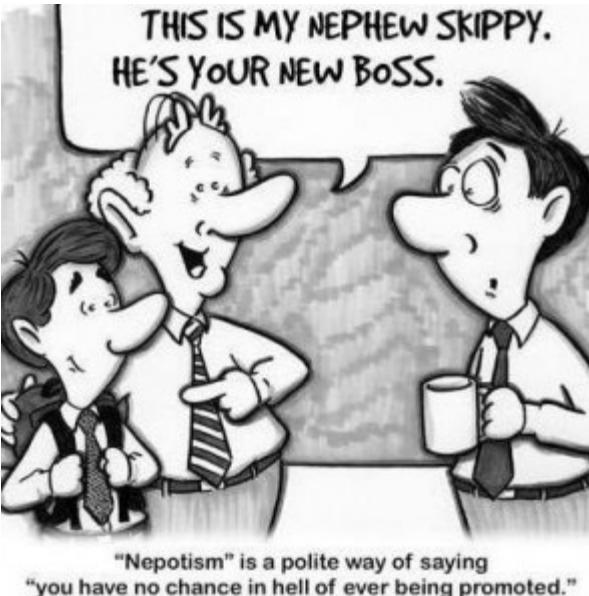


Papua New Guinea – Big Men of the Wantok



Building a meritocracy

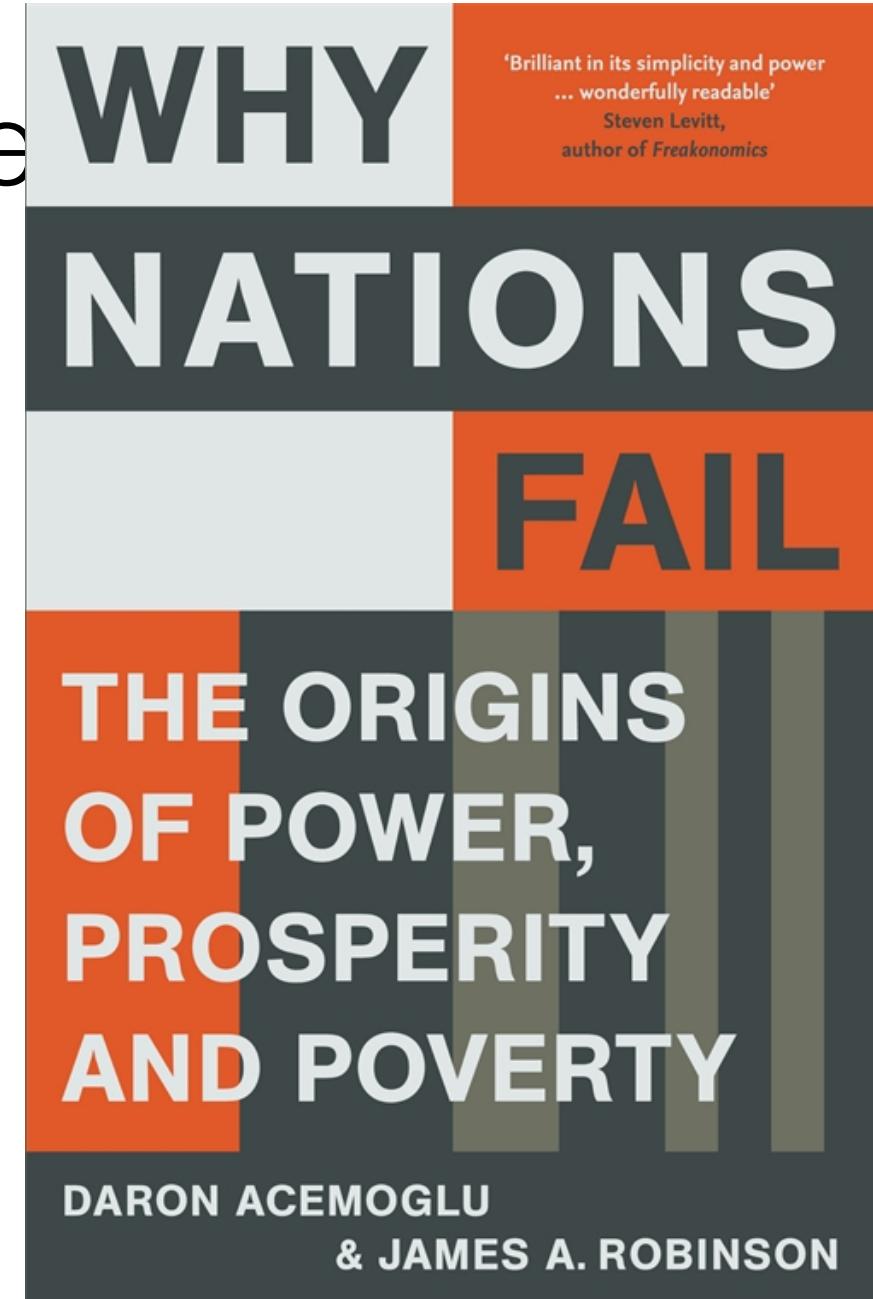
- Fukuyama: Humans are more or less biologically programmed to help their families and provide for their children.
- Nothing wrong with that in principle
- Except: when power is involved, leads to unequal opportunities



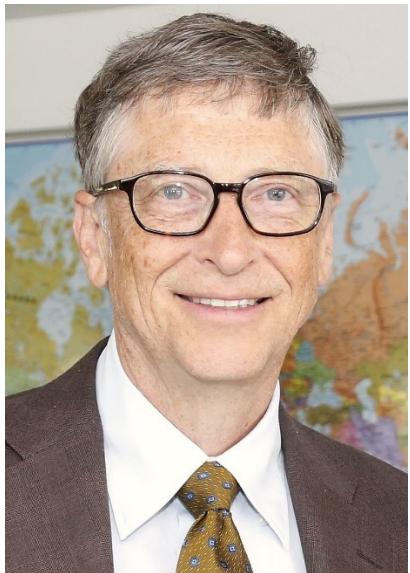
Limiting the power of the elite

Trust and development comes with “inclusive” institutions as opposite to “extractive” institutions.

Inclusive institutions aim to spread welfare and re-divide income among the entire population. Extractive institutions seek to profit only the elite and the ones in power



Explanation: The difference

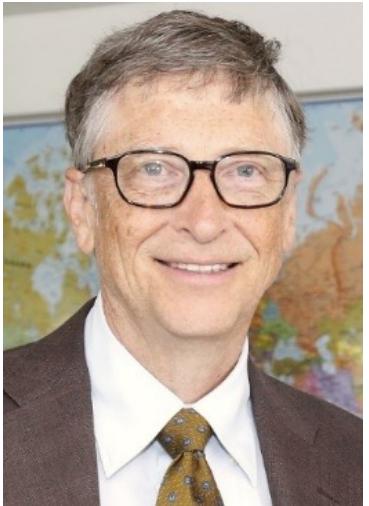


 Microsoft

 Walmart
Save money. Live better.

Kolomoyski, Pinchuk, Akhmetov

Some of the richest... How they earned money...



Bill Gates



Tim Walton



Brought innovations...



Carlos Slim



Brought a monopoly...



Microsoft felt the anti-monopoly regulations...



"Sir, I suggest we issue restrictive contracts, announce products that don't yet exist, link them to other products our customers don't want but are compelled to buy, and deliberately make our products incompatible with those of our competitors. Or is that too Microsoft?"

Carlos Slim's reaction when he heard
that someone put charges against him
for breaking anti-monopoly regulations.



Carlos Slim's reaction when he heard that someone put charges against him for breaking anti-monopoly regulations.



Characteristics for developing countries: Oligarchs trying to control as much of the market as possible.



Carlos Slim's reaction when he heard that someone put charges against him for breaking anti-monopoly regulations.



Carlos Slim's monopolistic business practices cost Mexico yearly 0.7% of economic growth. Bill Gates (Microsoft) on the contrary cause extra growth for the USA because of export of software.



Limitation of the power of the elite



Strong state

Rudolf Kjellén: Any successful state has more or less managed to gain autarky.

Strong state is required for true development.

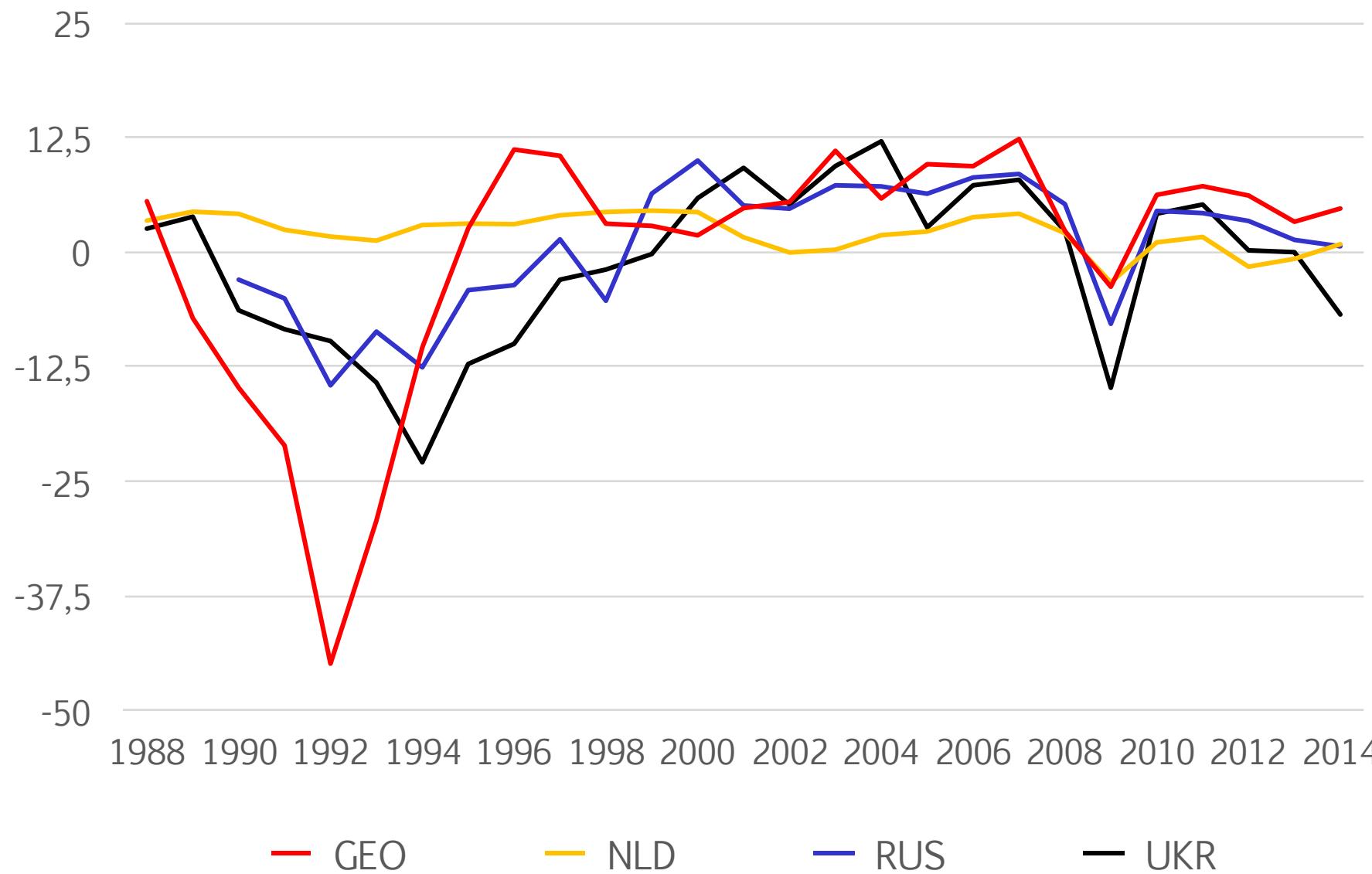
The state controls the society like the brain controls the body, by means of law and the military.



Necessary institutions for development

- **A strong state:** monopoly of power.
Opposite: weak state, “state in a state”, inability to collect taxes.
- **Rule of law:** impartial jurisdiction based on laws, not on power / influence.
Opposite: class justice
- **Accountable government:** transparent and possible to correct.
Opposite: dictatorship / tyranny, patron - client relation systems

Economic growth (%) of four countries (Worldbank)



Kom verder. Saxion.



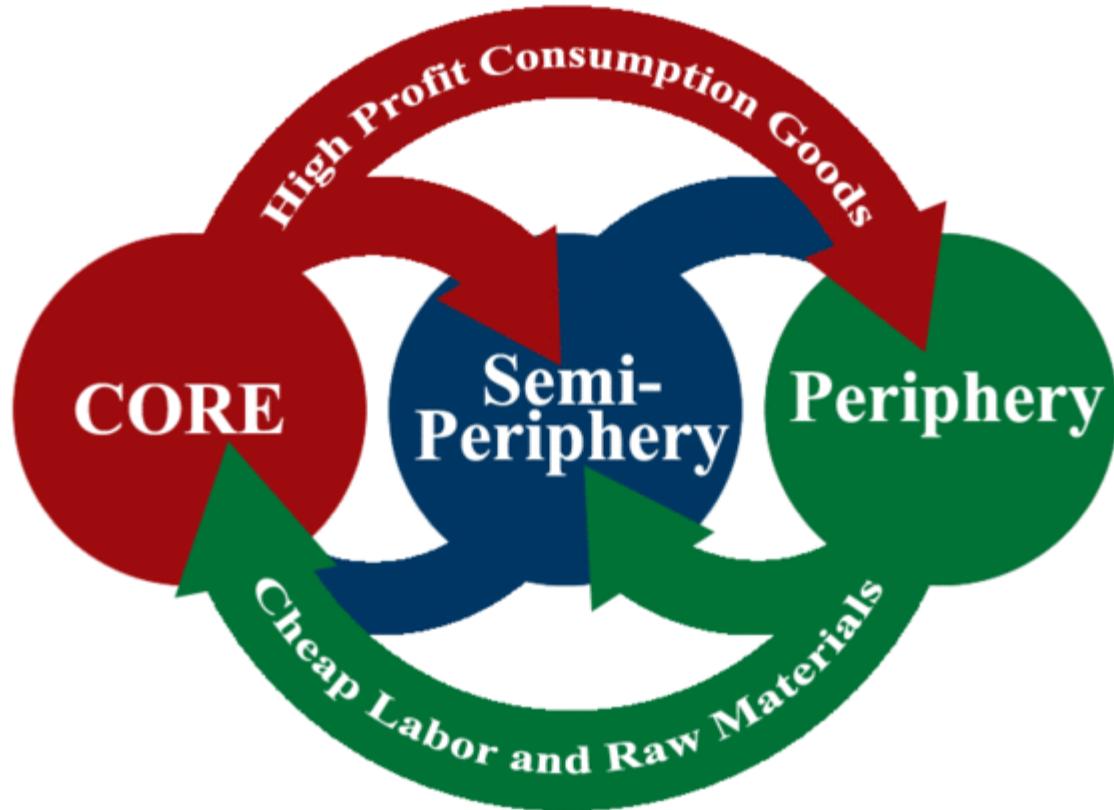
Part 3: Some thoughts about development



What does it mean in practice?



A stable World Economic System?



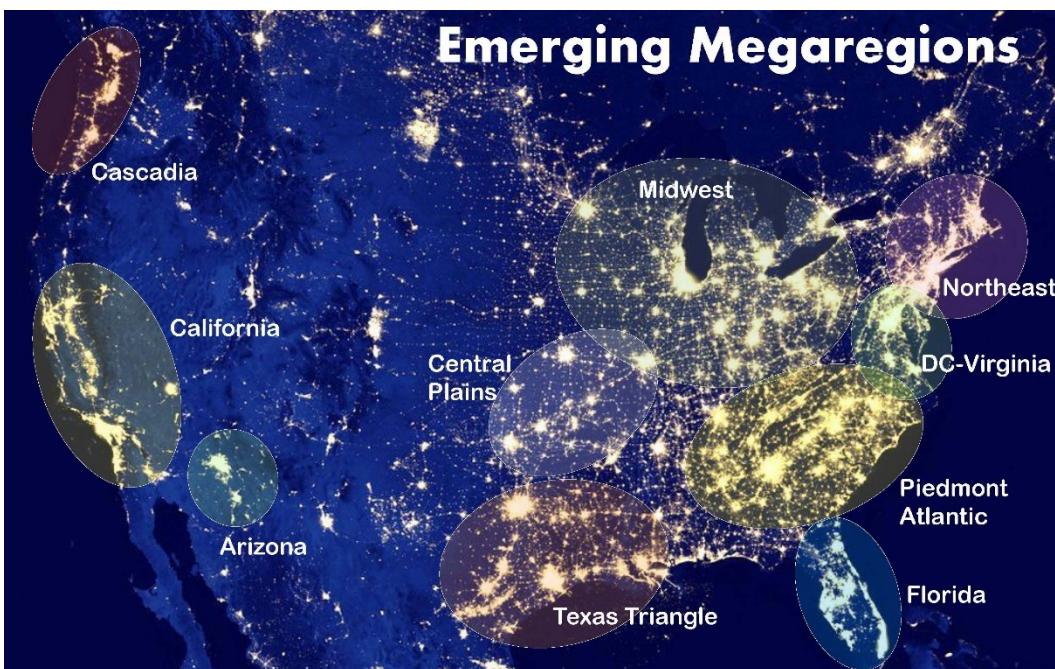
Wallerstein's World System Theory Model



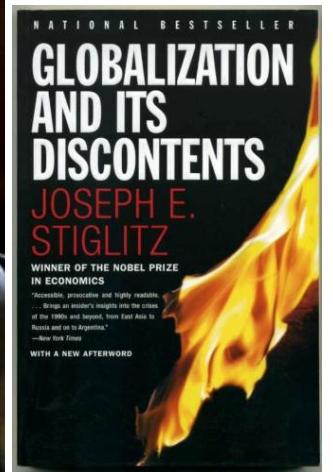
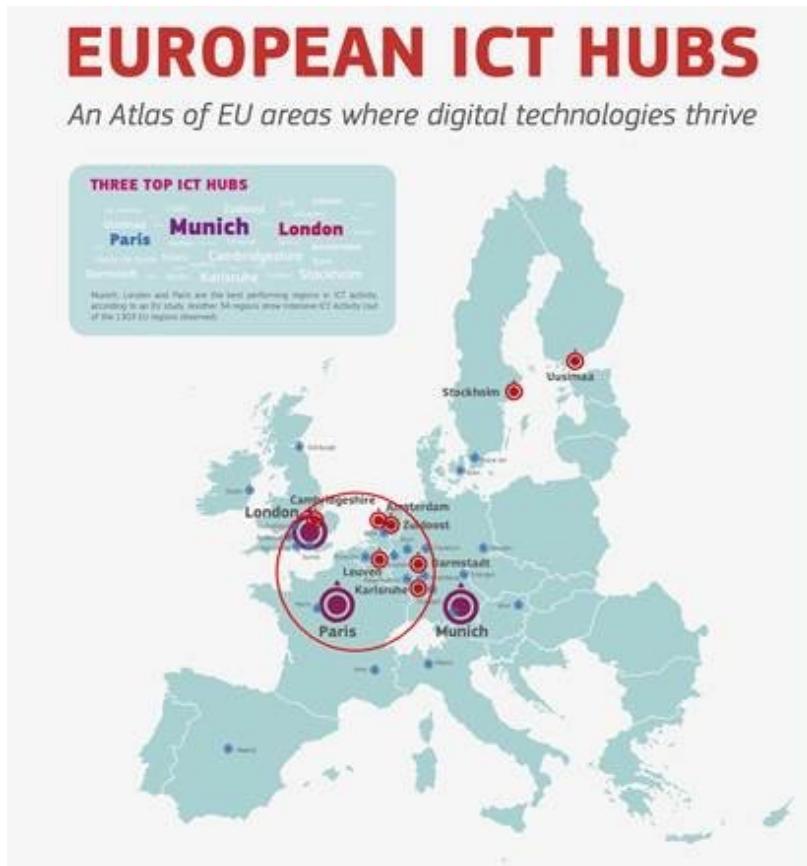
Wallerstein's idea: Unequal exchange between developed and underdeveloped countries

The clustering force

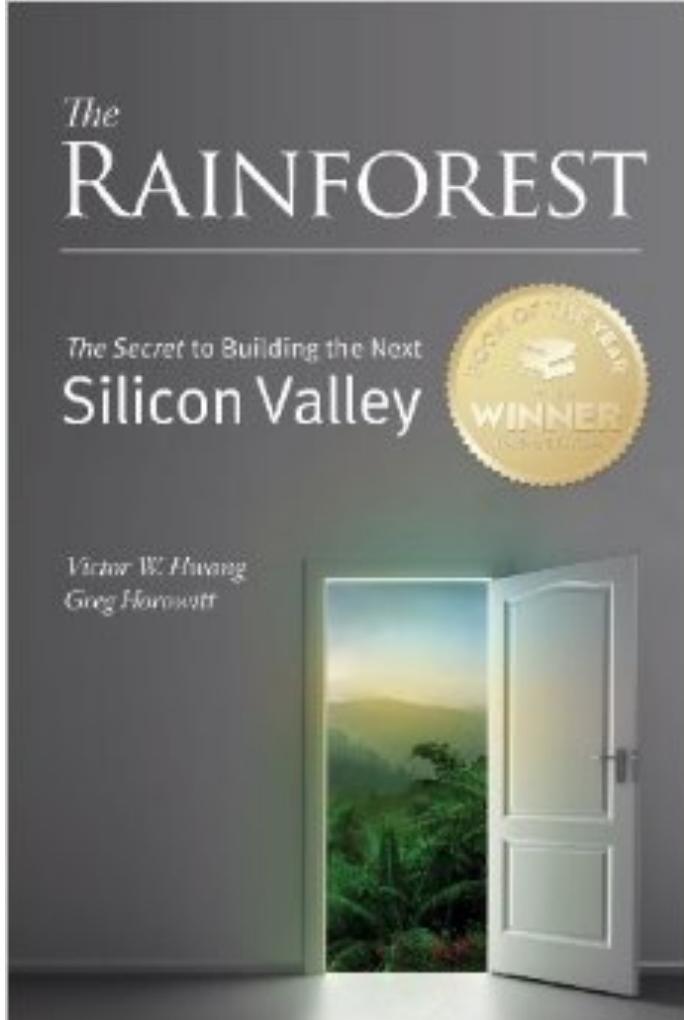
Richard Florida: Talent and development is more and more clustered in a smaller number of so called megaregions.



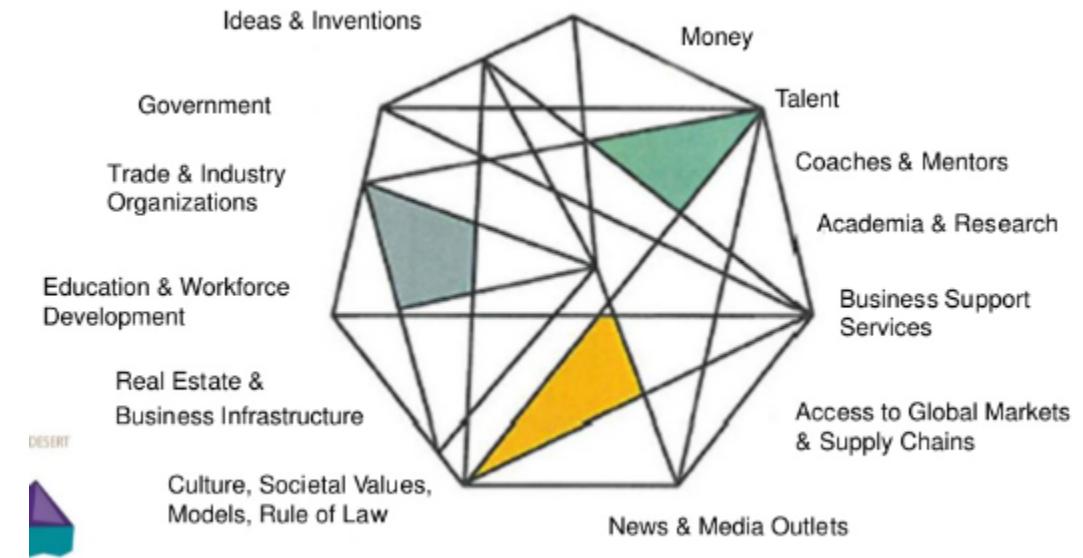
Internationally competitive clusters



“Rainforest” as explanation



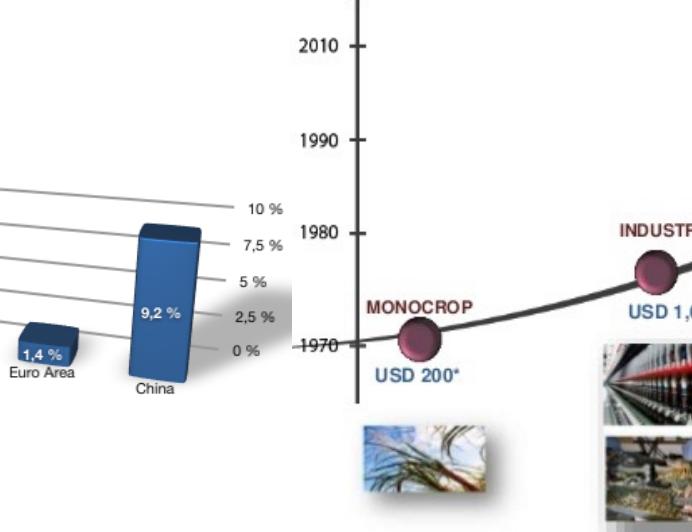
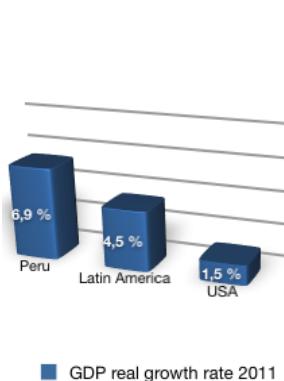
Hwang & Horowitz use the Rainforest metaphor to explain why some regions are successful in creating an innovative climate, while others are not.



What does it mean in practice?



What does it mean in practice?



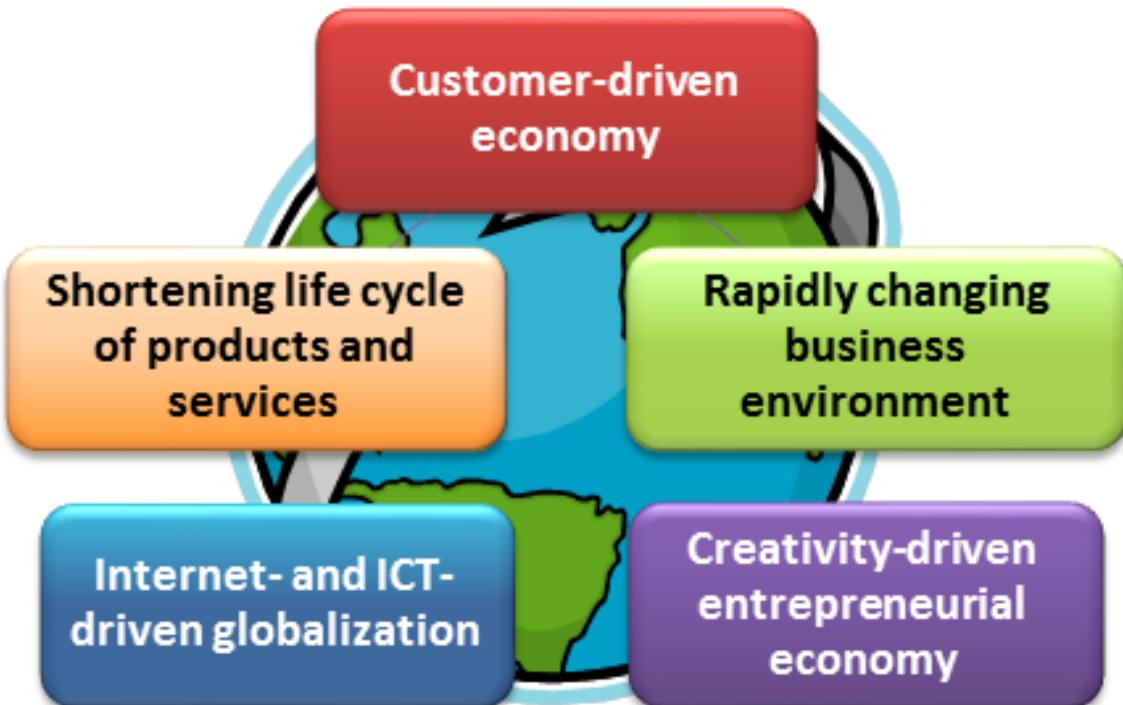
Economic Trajectory



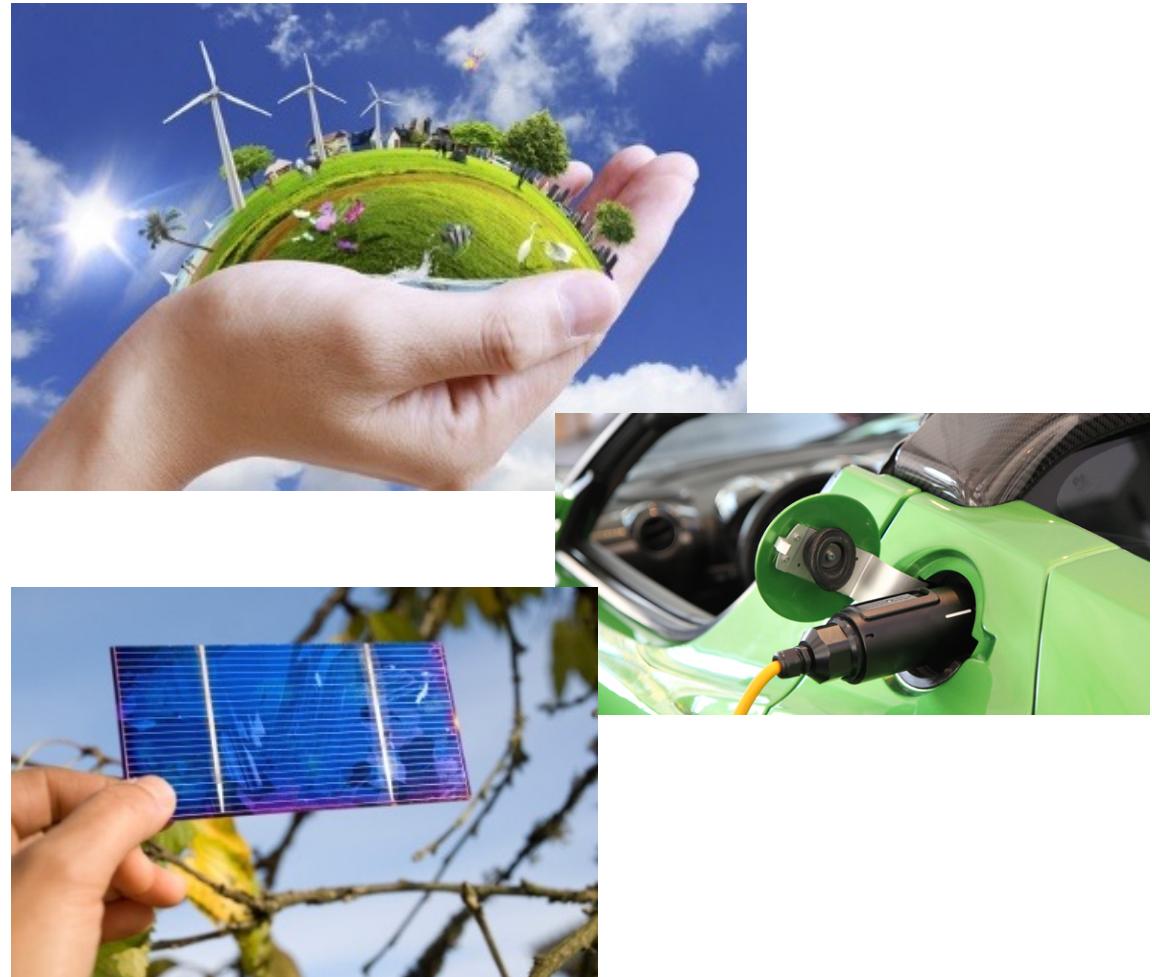
What does it mean in practice?



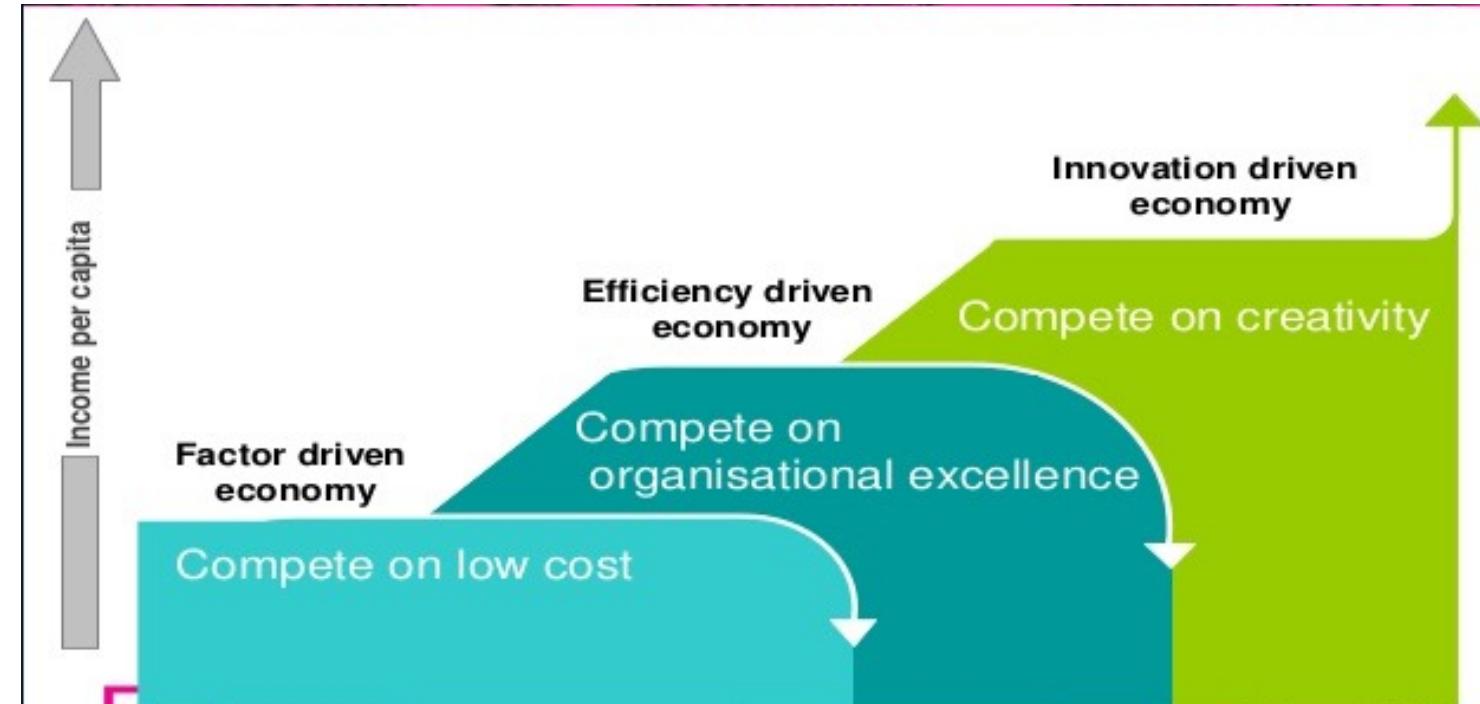
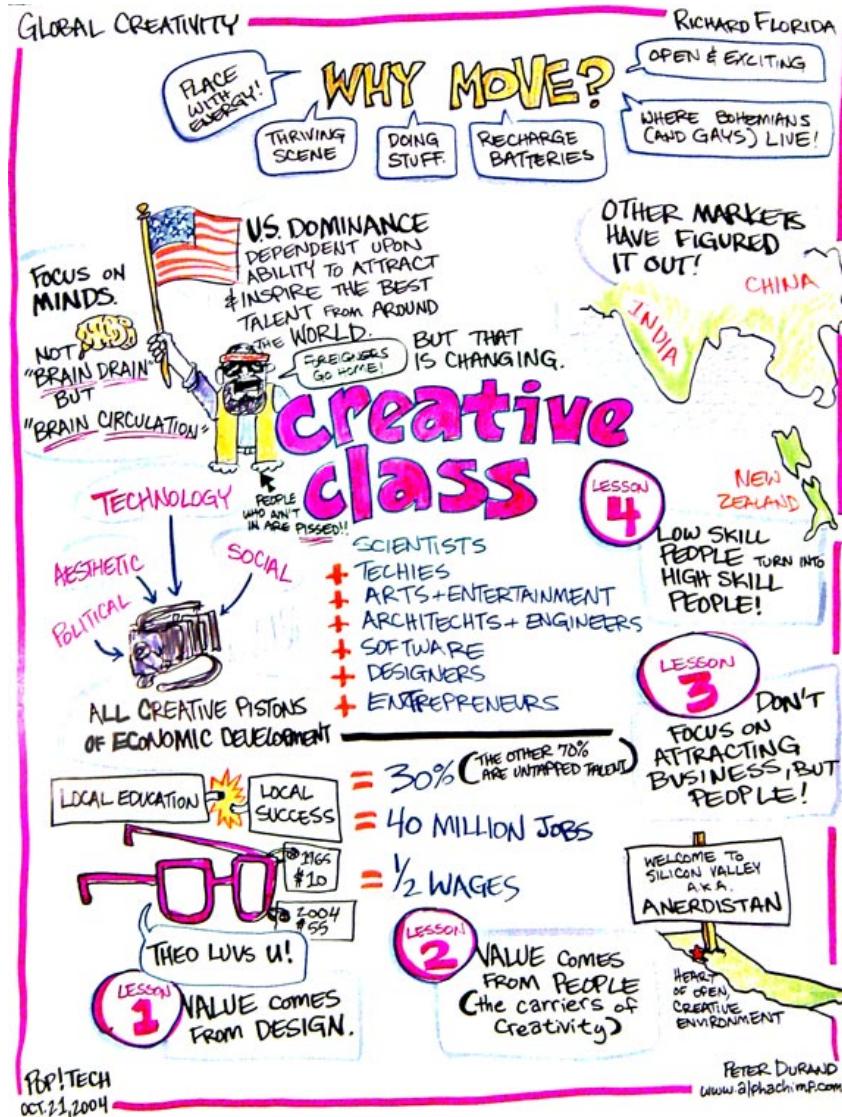
Modern Economy Key Features



1000ventures



The future - Creative economy?





Development strategies: Nauru vs. Singapore

Singapore's Economy 1960s to 2000s



Transitioning from one phase to the other

Why is it so difficult to follow Singapore or South Korea and make the transition to higher stages of development? The answer depends on who you ask:

1. Wallerstein: The World Economic system “forces” you to stay where you are as country.
2. Acemoglu & Robinson: The extractive nature of the institutions of society are probably hindering economic growth and creative destruction.
3. Hwang & Horowitz: Maybe there is no culture of innovation, no so called “Rainforest”.

More this afternoon