Trade, investment & human development

PUBLIC INTEREST

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I recently interacted with UNCTAD Secretary General Mukhisa Kituyi on the issue of trade and development in contemporary times, which stimulated some reflections on the subject.

Global exports must always equal global imports. The norm today is that some countries run trade deficits, others a trade surplus, and the net global result is zero. It would appear that following the rise of China, some world leaders, including the US President, do not like this. They would prefer that countries with large import balances run smaller trade deficits. In effect, this is a move to autarchy as in the limit; this would mean that every country would balance its exports and imports. Conventional theory would tell us that this would lead to efficiency losses, at least in a world where there are different factor and resource endowments.

The matter gets more complicated when we consider the role of finance and technology in the contemporary world. The rules of trade and investment are now more or less settled on the basis of a 50-year learning process for negotiating trade and investment rules. However, the rules of finance continue to be focused on regulating profit, maximising finance activities to prevent a global systemic collapse, and to maintain macroeconomic stability. There is little aspiration to try and secure better development results by establishing rules and institutions for the governance of finance. As I argued in my last column ("Financing the SDGs", October 5), the question of targeting non-concessional private finance toward securing the SDGs is not part of global negotiation. Since this is primarily about moving finance to public and private investments in developing countries, where they secure higher rates of return than at present, this is about a market failure that challenges both the theory of efficient markets and the theory of comparative advantage. Why do these theories fail when it comes to the export of capital to where it is most needed, and where returns are maximised? This finance dimension of the relationship between trade and investment is understudied.

Even if finance is forthcoming, it is important to recognise that there are domestic decisions to be taken to maximise its welfare impact. If trade is an engine of growth, does that mean that a rise in the export GDP ratio (even if accompanied by a rise in the import GDP ratio) will bring about a development transformation? Not necessarily. When countries like South Korea, Taiwan and China experienced export-led growth, there was as significant plough back into investments in health, education, public transport and urban systems. A portion of the dividends from export-led growth were invested in development. This fostered a development transformation, with the benefits of growth being devoted to better public infrastructure and human development. This, in turn, expanded the domestic growth base and fostered inclusive growth. In contrast, many middle-income countries did not do this and focused solely on maximising growth; as a consequence, they fell into the middle-income trap.

Other than finance, changes in technology are also fundamentally altering the trade-investment relationship. In the twentieth century, the same set of countries had concentrations of income, manufacturing prowess, capital and technology. Export-led growth allowed other countries with abundant supplies of labour to produce things that were lower down in the value chain, thereby maximising their labour comparative advantage. The subset of these countries that then invested in human development and structural change moved up the value chain. This is not the situation today. Emerging economies may well be locations where products involving advanced technology are manufactured. But the returns to manufacturing are much lower than the returns to technology. The key to the profitability of Apple, Microsoft, Boeing, and Airbus is their ability to innovate and develop products based on new technologies. The price of these products incorporates a large element of rent embodied in the intellectual property rights held by these corporations. These rents accrue to the countries where they are headquartered and where they patent their innovations, not to the countries where the products are manufactured.

Increased mobility of high-skilled human capital exacerbates this process. India may celebrate its' diaspora occupying important positions in major American and European companies and universities. But the value that these excellent minds of Indian origin produce is harvested not by India, but by the developed countries. India's investment in these minds is, in effect, sold cheap in the marketplace for knowledge where, with large amounts of innovation investment, they deliver huge returns. Thus, countries like India are doomed to constantly invest in human capital, only to see it sucked away into the techno-industrial complex. A former senior official of the Rajasthan government told me that for every 3,000 doctors that graduate in that state annually, only 200 apply to work in the public health system. Thus, our domestic systems atrophy as our investment in human capital migrates to earn higher returns elsewhere. The development implications of these human capital exports are unsettling. Even as we celebrate their success, we have to understand that they are part of a system where their expertise generates knowledge rents for the rich, at the expense of domestic capacities for development transformation.

These reflections do not currently resonate in bilateral or multilateral policy conversations. If domestic and global economic stability and harmony are to be maintained and fostered, I think it is important that they do.

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