

A vertical photograph of a busy city street, likely New York City, showing a row of multi-story buildings on the left. In the foreground, several cars and a yellow taxi are parked along the curb. People are walking on the sidewalk. The sky is overcast.

Government and Economic Growth

Last Time

1 Global market is essential for economic development:
Comparative advantage;
Scale economies

2 Export-led economic growth in Asia-Pacific economies: export promotion+assembly+global value chains

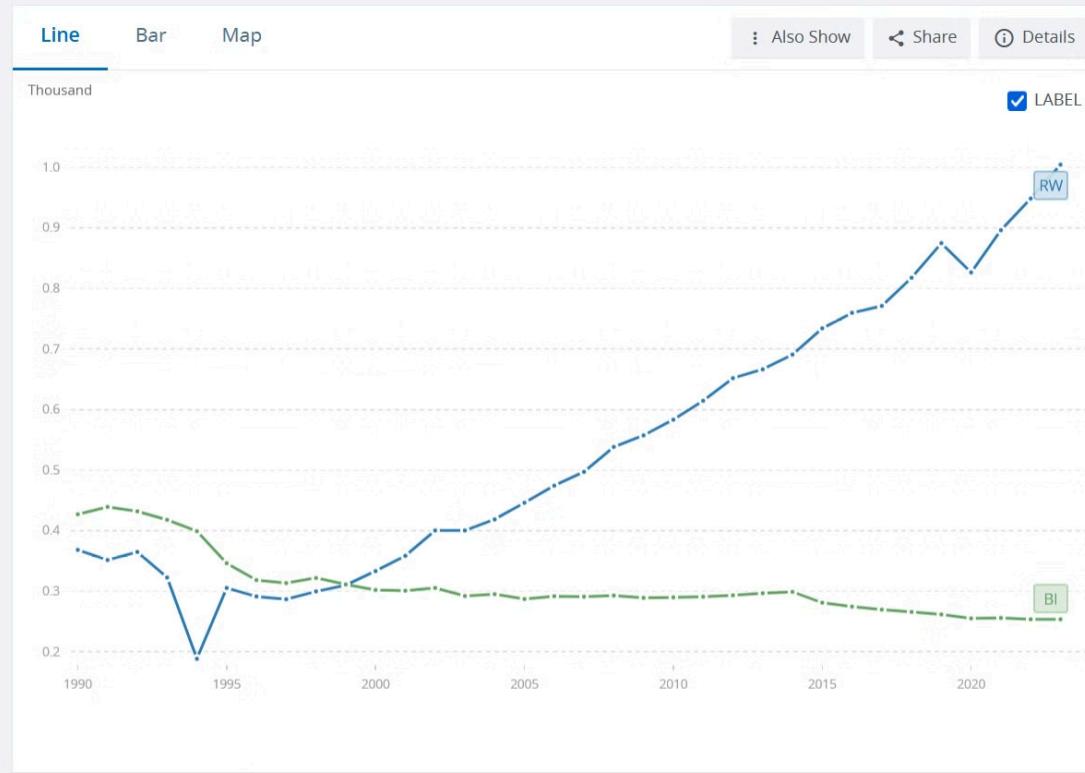
3 Disruptions of GVCs: the US-China trade wars

Rwanda vs. Burundi in Economic Growth

GDP per capita (constant 2015 US\$) -

World Bank national accounts data, and OECD National Accounts data files.

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Data source: <https://data.worldbank.org>



Kagame and Rwanda's Growth Miracle



Paul Kagame (1957-)

- Leader of Rwanda since 1994
- Vision 2020
 - Infrastructure
 - Foreign direct investment
 - Education
 - Reducing red tape for businesses
- Won four presidential elections: >90% vote



Governments and Economies: Various Models

We're great at judging models, but at the end of the day, it's about solving our own problems.



Government vs. Market

What's special for the government in an economy?

What are the roles of government in an economy?

Necessities

- Public services
- National defense
- Infrastructure

Interventions

- Regulations
- Redistributions
- Subsidies or public enterprises



Market Failures

1 Externalities

2 Public goods

3 Monopolies

4 Coordination failure

Externalities

- 1
- 2
- 3

Effects of a market exchange on a third party who is **outside**

Positive vs. Negative Externalities

What are the consequences of externalities?



Example: Congestion Pricing

- Externality: Individual drivers do not consider their impacts on traffic congestion and air pollution in city centers
- Policies?





Public Goods

Non-excludable + Non-rivalrous

- Which of the following are public goods?
- | | | | |
|---|-----------------|---|------------------|
| 1 | Road system | 2 | Clean air |
| 3 | Social security | 4 | National defense |
| 5 | IP protection | 6 | Public education |
- Why do public goods (often) rely on government provision?

Monopolies

Market Power

- In a competitive market, firms have little impact on market price
- When firms have market power, they can increase prices by reducing supply

Innovation

Compared with firms in competitive markets, monopolies are in lack of incentives for innovation

1

2

3

4

Consumers' welfare

Consumers lose from market power

Regulation

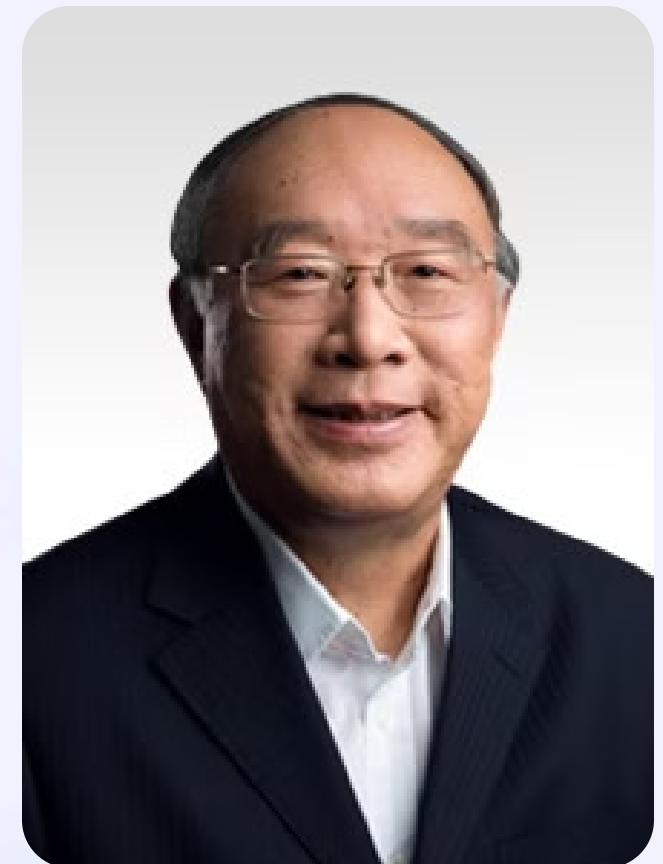
Anti-Trust Laws

Coordination Failure

Example: Foxconn in Chongqing, China

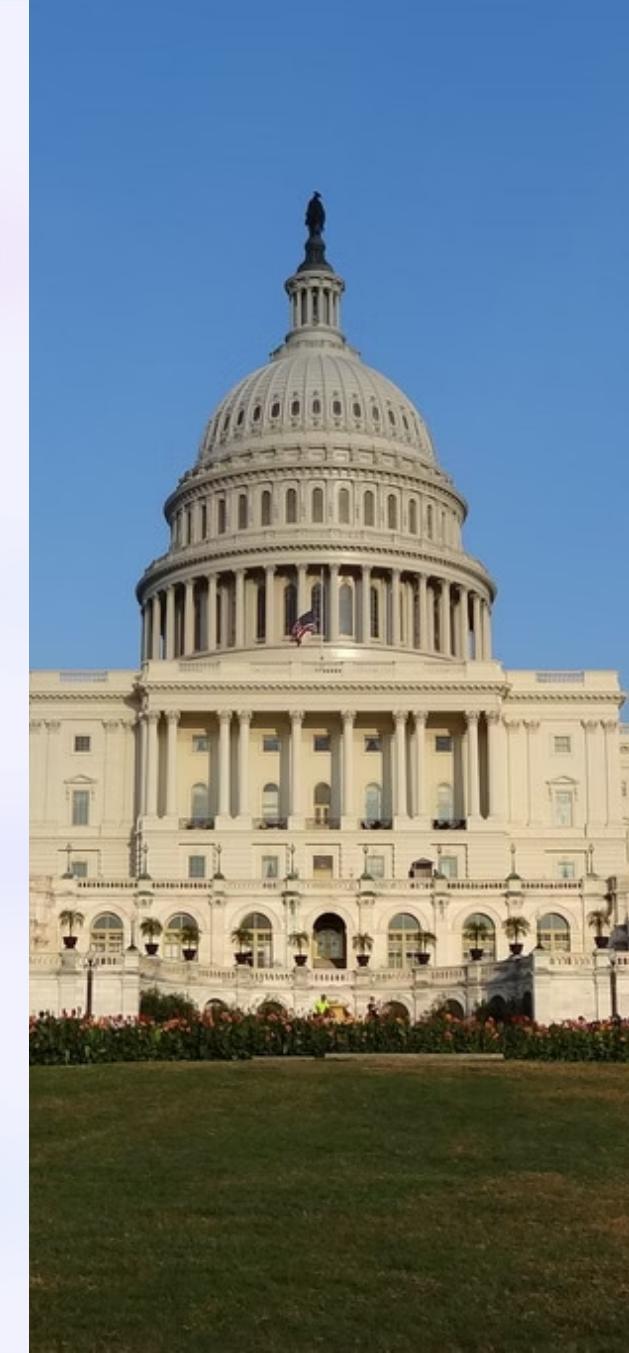
- The largest assembly firm for Apple
- Large and complicated **networks of suppliers**

Qifan Huang, former mayor of Chongqing, China



What might be wrong with the "market-failure" argument?

- 1 "Government can intervene" ≠ "Government should intervene"
- 2 "Market failure" ≠ "Government success": **Corruption, inefficiency, and misguided policies**
- 3 The appropriate level and form of intervention that aligns with the nuances of the economic context



Government and market: Three models

- 1 Anglo-Saxon model
- 2 European model
- 3 Asian (Japanese) model



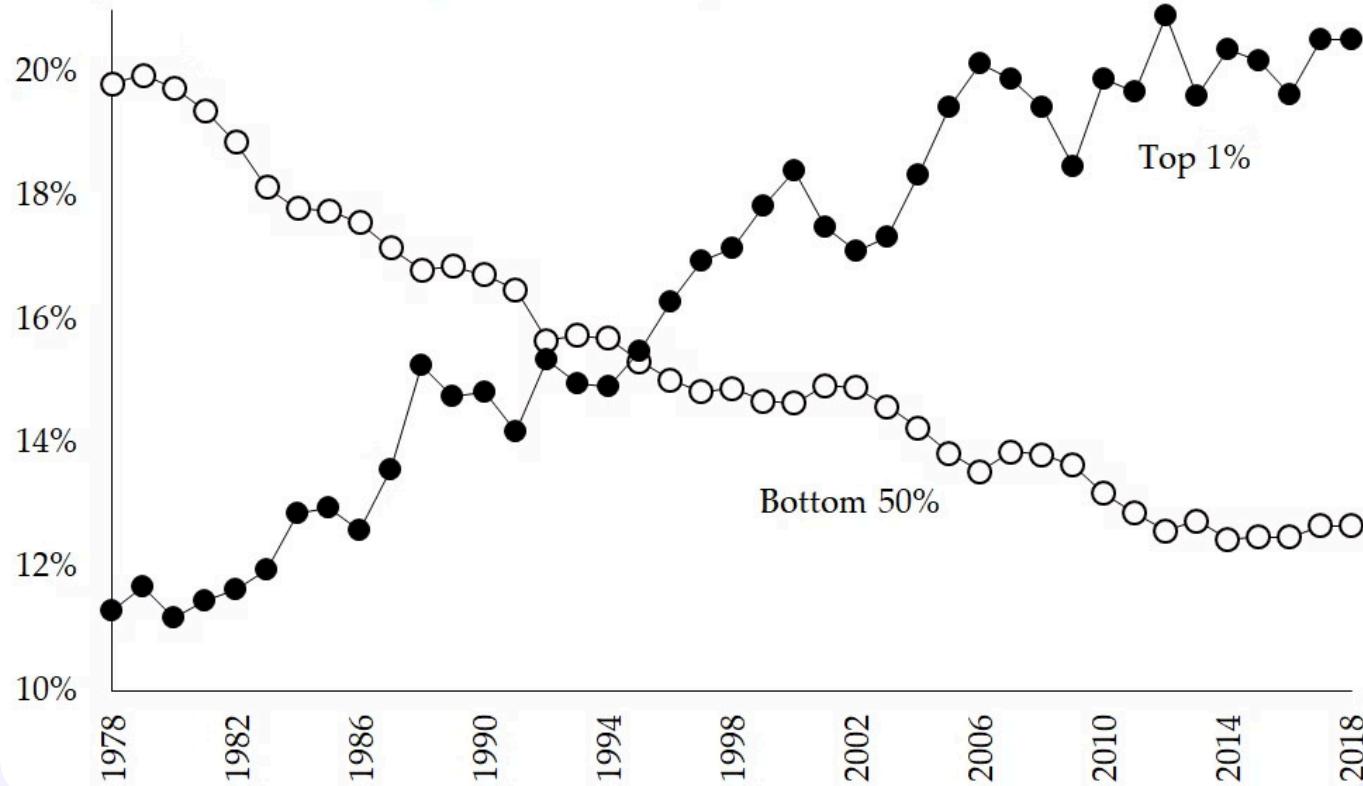
Anglo-Saxon model: Features

- 1 Low levels of regulation and taxation
- 2 Public sector provides minimal services
- 3 Strong private property rights and contract enforcement
- 4 Overall ease of doing business
- 5 Low barriers to free trade
- 6 Liberal and free markets

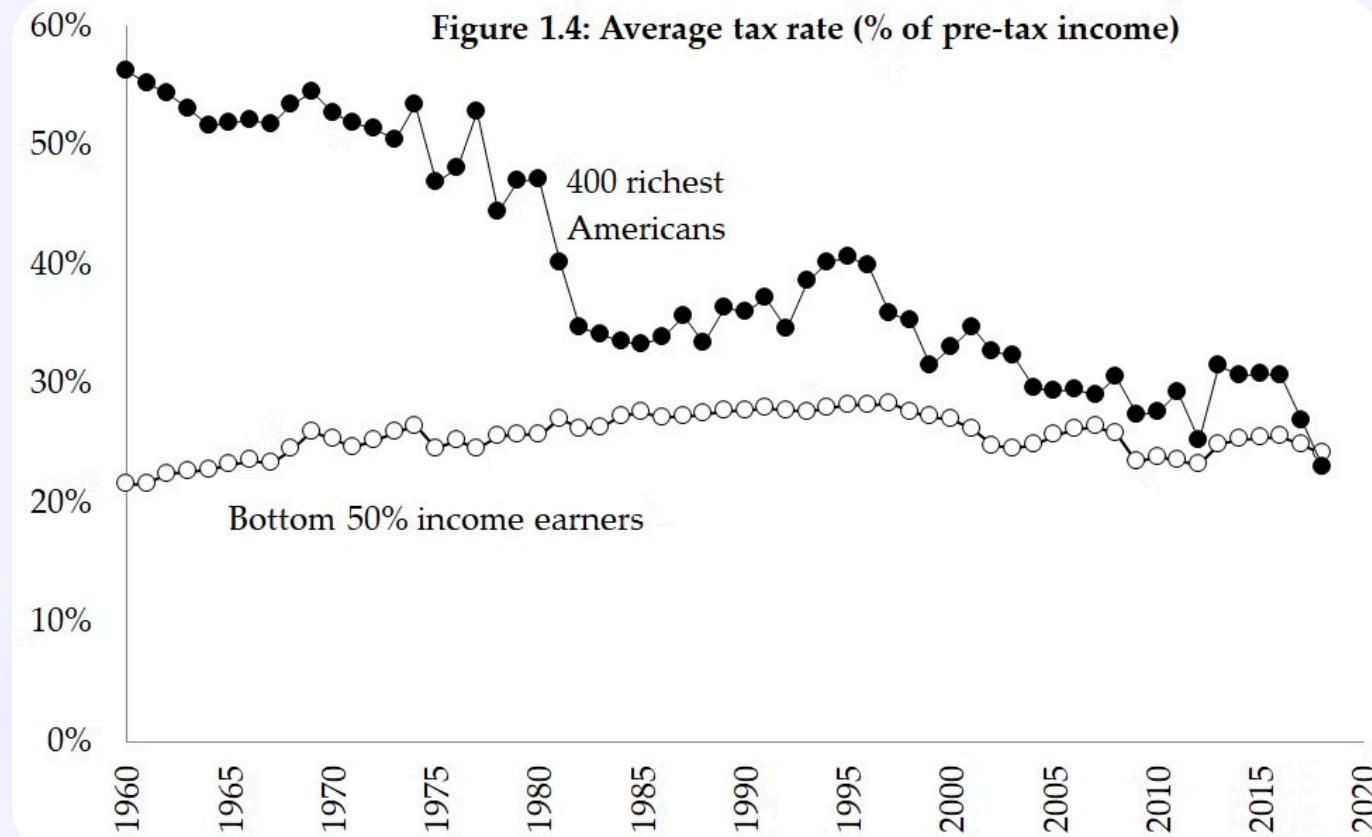
Countries and economies?

Pro-Business

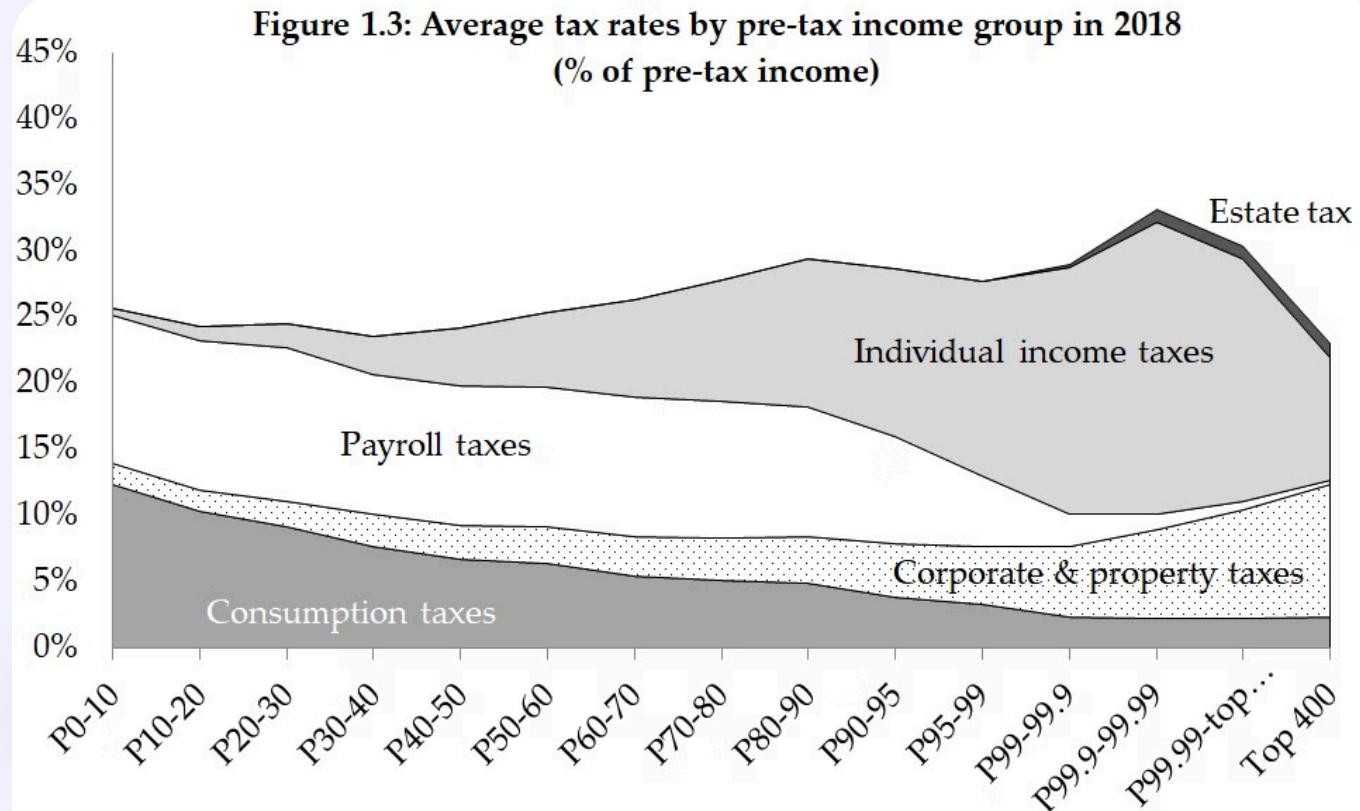
Figure 1.1: Share of pre-tax national income



Pro-Business

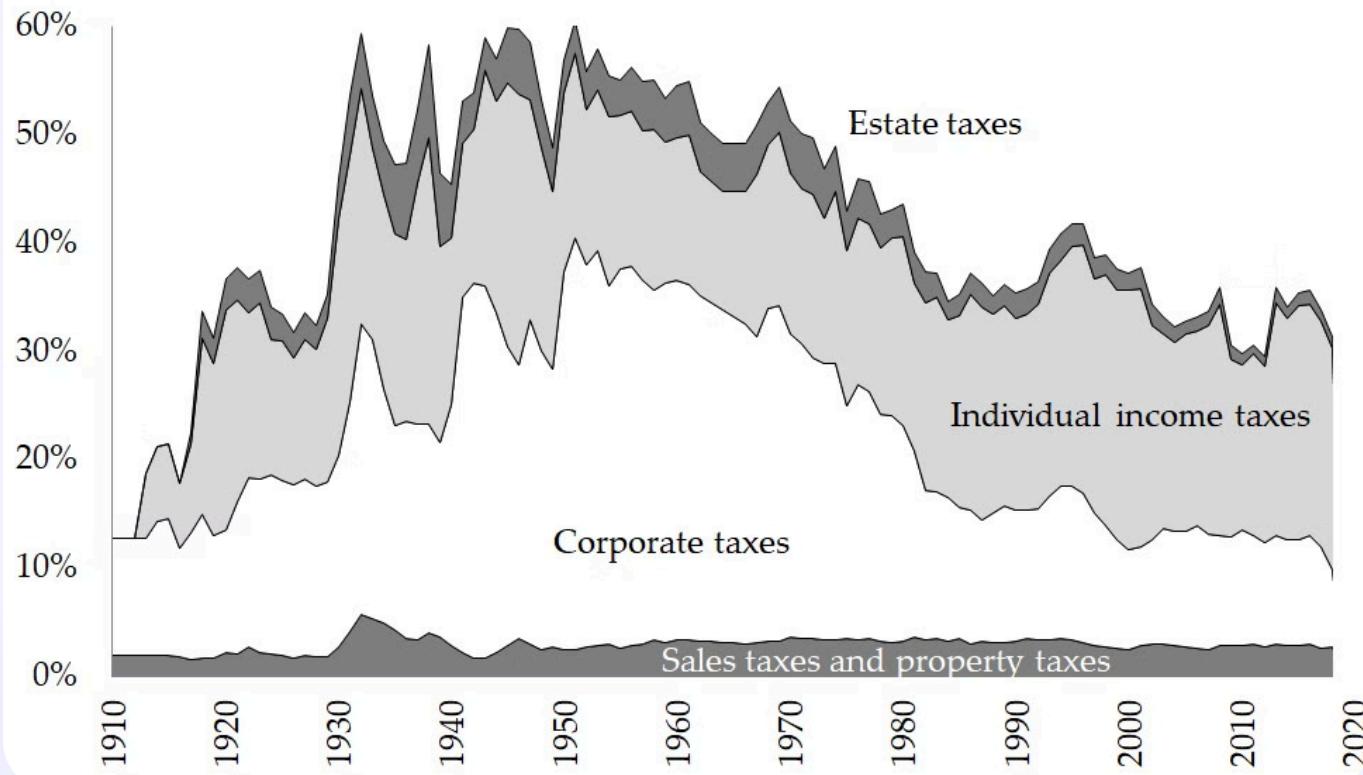


Pro-Business



Pro-Business

Figure 2.3: Average tax rate of the top 0.1% (% of pre-tax income)



Emmanuel Saez and Gabriel Zucman (2019) The Triumph of Injustice



European (Social) Model

- 1 Employment regulation
- 2 Social protections
- 3 Social inclusion
- 4 Democracy

Typical Policies?

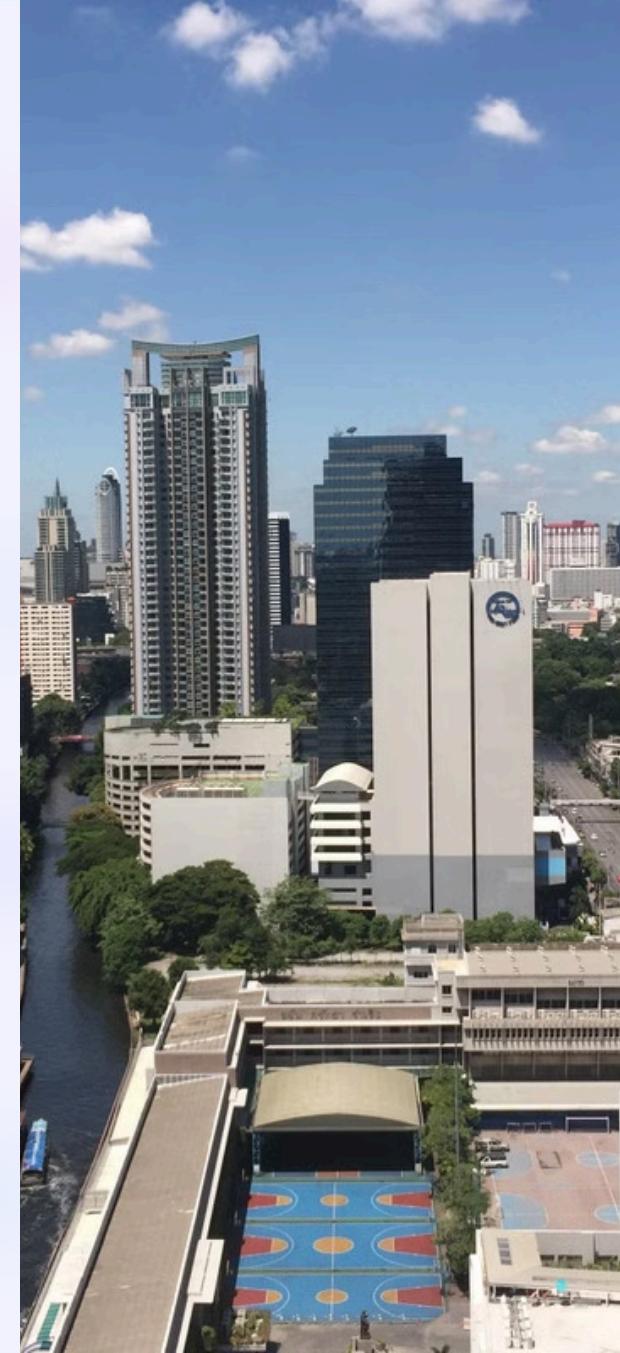
East Asian Model

Joseph Stiglitz

The key lesson of the remarkable and sustained success of Asia-Pacific economies was that **government undertook major responsibility for the promotion of economic growth**

Strategies: Pro-Production + Specific Industries

- Saving and investment
- Industrial policies
- Export-oriented development
- Human capital investment



Savings and Investments



- 1
- 2

Large fraction of GDP ⇒ Government

High saving rates

Government investment

- Public services
- Industrial subsidies

Industrial Policies and Their Impact

Strategic Sectors

1 Features of strategic sectors?

2 Should we trust the government to pick strategic sectors?

Policies to support strategic sectors?

Export-Oriented Development

1

Pro-Openness

- Imports ⇒ Exports
- Inward FDI

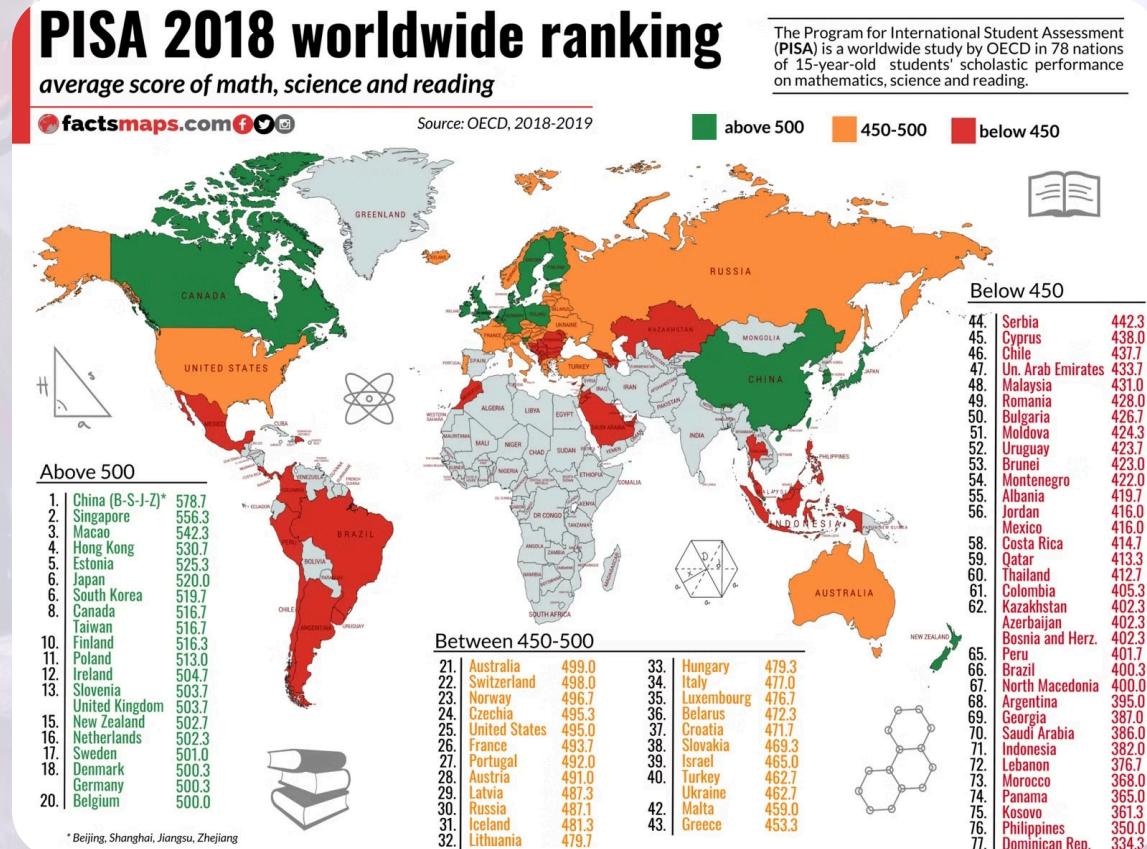
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Competitive Advantage

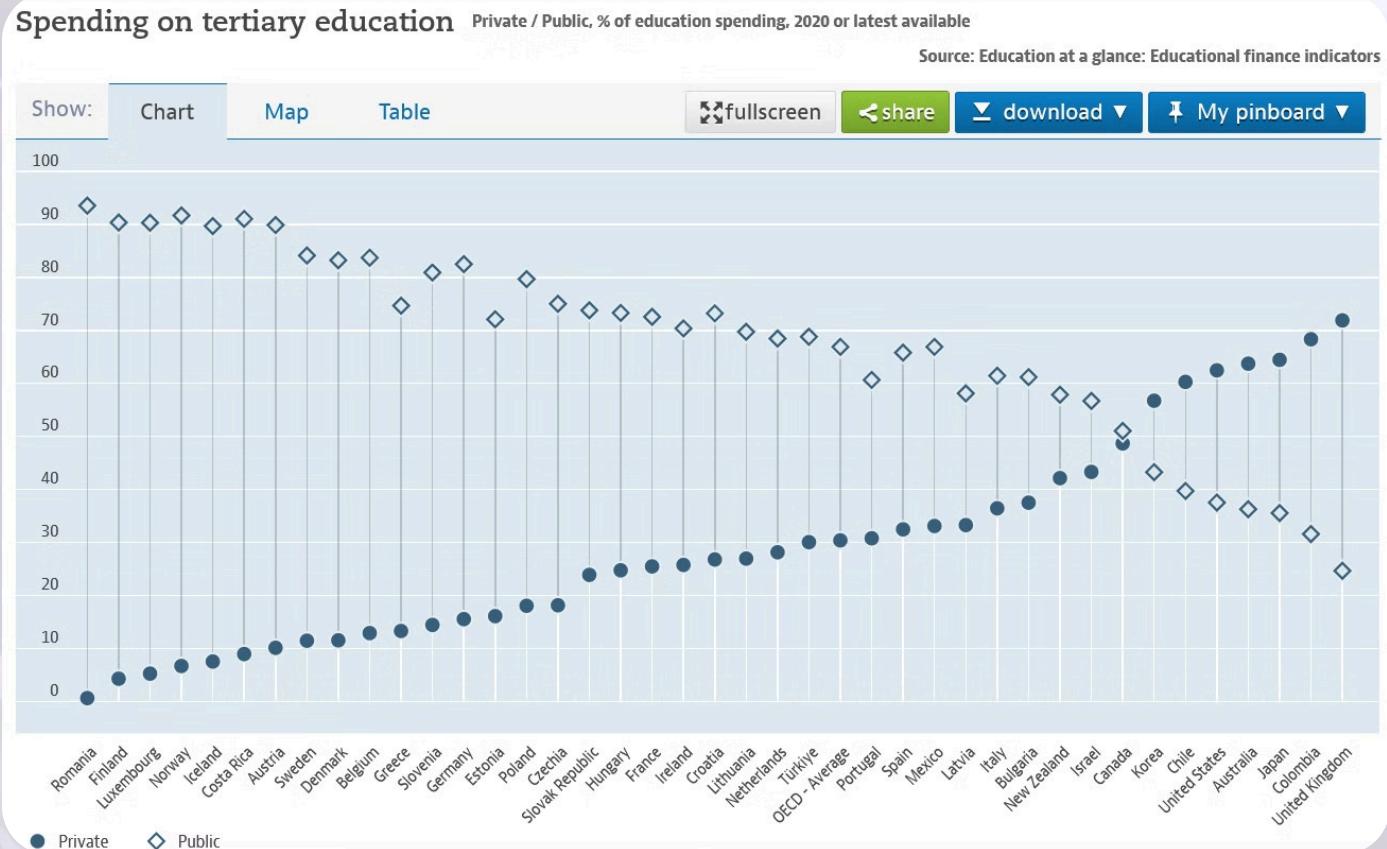
- Selected industries
- Dynamics: deliberately create new comparative advantage



Investing in Human Capital



Investing in Human Capital



Discussions: Which models do you want to live in?

- 1 Anglo-Saxon model
- 2 European (Social) Model
- 3 East Asian Model