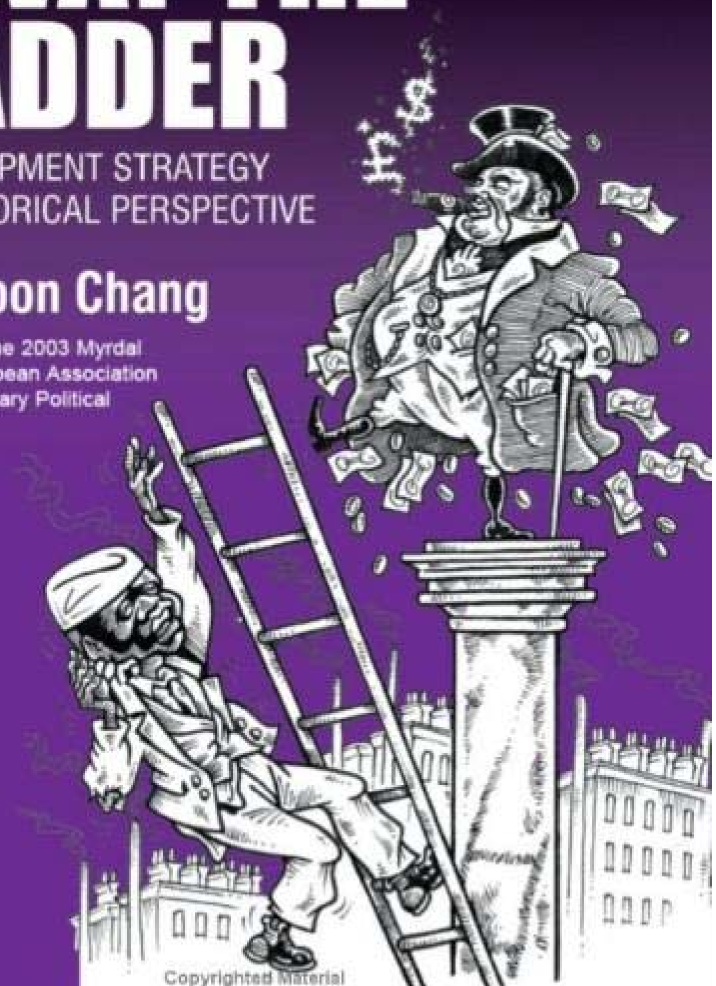
KICKING AWAY THE LADDER

DEVELOPMENT STRATEGY IN HISTORICAL PERSPECTIVE

Ha-Joon Chang

Winner of the 2003 Myrdal Prize, European Association of Evolutionary Political Economy



'Probably the world's most effective critic of globalization'
MARTIN WOLF, *FINANCIAL TIMES*

'Lucid, deeply informed'
NOAM CHOMSKY

BAD SAMARITANS

THE GUILTY SECRETS OF RICH NATIONS & THE THREAT TO GLOBAL PROSPERITY

HA-JOON CHANG

Development History of Rich Countries I

- **High degrees of protectionism**
  - Before WWII, average industrial tariff 40-50% in Britain and the US (today's developing countries average 10%)
  - Even countries that had relatively low tariffs, some sectors had high protection
    - Belgium in the mid-19th century: 10% average tariff rate, but 30-60% tariff for textiles, 85% for iron
  - Quantitative restrictions (bans, quotas)

- **Subsidies widely used** for all purposes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Development History of Rich Countries II

- **FDI was heavily regulated**, especially in natural resources and services.
  - Until the mid-20th century, the US didn't allow foreigners to log in public land or run coastal shipping, while banning foreign shareholders from voting in shareholders meetings for banks
  - In post-WWII period, Japan virtually banned FDI
  - Finland classified all firms with more than 20% foreign ownership as 'dangerous enterprises'.

Development History of Rich Countries III

- **Intellectual property right protection was lax, to put it mildly.**
  - Allowed **patenting of foreigners' inventions**
  - Most of them did not protect **product patents in pharmaceuticals** and chemicals
  - **Switzerland** and **the Netherlands didn't even have a patent law** until the early 20^{th} century.

Shrinking Policy Space

- There are **many** industrial policy **measures** that **can still be used legally** under the WTO system.
  - For some measures, international rules do not apply or do so rather leniently to developing and the least developed countries (e.g., export subsidies)
  - Some policy measures are inherently domestic in nature and thus not subject to international agreements.
    - As a rule of thumb, with regard to multilateral obligations, **if a policy measure does not affect exports or imports, it does not fall directly under WTO laws and should be allowed**.
  - Also, ambiguities in certain rules or their application can create further scope for pushing certain policies till they are detected or challenged.

The WTO – Tariffs

- WTO member countries are **only required to ‘bind’** (that is, set the upper limit to) at least some of their **tariffs**.
  - Indeed, not all of them have bound all of their tariffs – there are **many members of the WTO (many of them in Africa) that have bound virtually none of their tariffs**.
  - Even many of the countries that have bound their tariffs have bound them **at quite high levels**.
- As **the current levels of tariffs** in most countries are **well below their bound levels**, they can raise tariffs.
- It is also possible (albeit difficult) to **re-negotiate bound tariffs** for some products.
- Developing countries can also apply **extra tariffs** or even quantitative restrictions **to address balance of payments problems**, although they require elaborate procedures.

The WTO – Subsidies

- Contrary to common misperception, the WTO **does <u>not</u> ban any subsidy other than export subsidies** (except for the LDCs and other poor countries) **and subsidies requiring local contents**.
- Of course, all subsidies are ‘actionable’ – that is, they canbe challenged in a WTO dispute and, should the challenge be successful, be removed.
  - However, it takes a few years before a subsidy is challenged and ruled illegal.
- There are **subsidies that can be more safely used**.
  - Subsidies for R&D, upgrading of disadvantaged regions, and developing environmentally friendly technology have hardly ever been challenged, at least partly because they are subsidies preferred by rich countries.

The WTO – FDI Regulation

- **TRIMs prohibits domestic content requirements** and **foreign exchange balancing requirements**.
- **But** it **permits many other measures** – those related to joint venture, technology transfer, or limitations on foreign equity ownership.
  - Moreover, many countries are still using thinly disguised local content requirements, for example, in relation to the oil and gas sector, so developing countries should more actively explore such possibilities.
- **GATS** does restrict countries' ability to restrict FDI in services.
- But developing countries have made few commitments, so their **room for manoeuvre is much greater** in this area, including in relation to local content requirements.

In Defence of Multilateralism

- Thus, the **restrictions** on policies that countries need for economic development, imposed by the WTO, are **considerable but not overwhelming**.
- **However, bilateral (or regional)** trade and investment **agreements** between developing countries and developed countries, especially the ones with the US, are ‘WTO-plus’, so they **severely restrict policy freedom**.
- This is not to say that the current system is good enough.
- The system should be reformed in a more pro-developmental way so that developing countries are provided greater policy space to pursue policies that are more suitable their stages of development.