CHAPTER SIX

The 'Rise of the South'

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Recent debates about the 'Rise of the South' (RoS), global convergence and North–South decoupling have been driven by the perception of far-reaching transformations in the global economy in the last 30 years. These views have been supported by the impressive economic performance of several developing economies (DEs) recently, especially the so-called BRICS (Brazil, Russia, India, China and South Africa), and by the relatively shallow downturn experienced by the latter in the wake of the global crisis starting in 2007, in contrast with the deep contraction and the protracted slowdown in many advanced economies (AEs).

The size, importance and perceived success of the larger DEs, and the striking growth achievements of many smaller economies, have lent support to the argument that the world is 'turning upside down': the economic and political supremacy of the West is being eroded rapidly, changes in global governance will inevitably follow, and the next generation of world-leading economies can already be identified.

Many political scientists and international relations scholars have expressed concerns about the potentially destabilising implications of these transformations. This chapter does not address these issues (see Klassen, Chapter 7 in this book). It focuses instead on the economic debates around global convergence. It shows that, despite the potential significance of the RoS, the conventional narrative of this process and its implications is flawed. In contrast, a critical political economy analysis suggests that the global economy is defined by shifting patterns of unevenness at the levels of firms, production chains, countries and regions, and that there is no automatic tendency for countries to converge. Outcomes depend on circumstances, economic policies, the strength of social movements and global constraints. Examination of the structures and processes included in the 'RoS' can help to illuminate the achievements, limitations and contradictions of economic development policy in the age of neoliberalism, and inform the search for democratic alternatives.

This chapter has six sections. The first reviews the mainstream literature on economic growth and convergence, and the evidence of long-term convergence. The second summarises the long-term patterns of divergence in the world economy, in the light of the concepts of primary and secondary uneven and combined development. The third focuses on the development policies imple-

mented in the post-war period, their impact on global inequality, and recent DE growth performance. The fourth assesses the period since the onset of the global crisis, and discusses the predictions of North–South 'decoupling'. These sections show that moments of convergence have often been decontextualised and exaggerated in support of a neoliberal policy agenda. The fifth examines three possible drivers of convergence: transnational production networks, the 'flying geese' paradigm and industrial policy. The final section discusses the conditions for promoting democratic (pro-poor) development strategies in the South, supporting a socially desirable process of convergence.

Long-Term Patterns of Growth

Evidence of sustained economic growth in the Northern 'core' of the world economy since the Industrial Revolution, in contrast with slow growth or even decline in the Southern 'periphery', has triggered several waves of debate about the scope for global convergence.

In the early and mid-20th century, Thorstein Veblen and Alexander Gerschenkron advanced the intuitively appealing idea that early developers create technologies which others can learn, purchase or steal. Since the adaptation of new methods of production is likely to be cheaper than their discovery, late-comers have an inbuilt advantage and can fast-track their development process. Consequently, capitalist economies can converge rapidly in terms of per capita income, living standards, productivity and technology, dispensing with the need for socialist revolutions or even large-scale state intervention. These insights were incorporated into the growth literature through the work of Evsey Domar, Roy Harrod, and especially Robert Solow. Solow's influential growth model became especially prominent, and was associated with the notion of *unconditional convergence* (for a more detailed presentation, see Saad-Filho, 2013).

Despite their econometric sophistication, most mainstream studies of unconditional convergence have been unpersuasive. They tend to suffer from several limitations, including questionable data sets, inadequate models, and the mutual determination of parameters and outcomes. Their closed economy assumptions rule out international trade, flows of capital and labour, technology transfers and institutional learning (including the effect of Washington Consensus-type policy conditionalities), even though neoclassical theory claims that global integration is a key driver of growth.

By the mid-1970s most observers had accepted that poor countries were not actually converging; moreover, the distribution of income was clearly deteriorating across the developing world. Despite these obvious limitations, the Solow model has remained influential, because it is simple, optimistic, and follows directly from the postulates of mainstream economics.

The weaknesses of traditional growth theory, and increasing recognition of global divergence, helped to popularise the alternative mainstream view that

convergence is both rare and policy-dependent, or that it is *conditional*: each economy tends towards its own income level in the long run, depending on their policies, institutions and circumstances. In order to converge, DEs must adopt the 'correct' economic policies and implement the 'necessary' structural reforms, which are invariably inspired by mainstream economics. These insights have been incorporated into competing variants of endogenous (new) growth theory since the mid-1980s.

The controversies between supporters of conditional and unconditional convergence have been inconclusive, and, while some authors estimate progressive reductions in global inequality since the Second World War, others find a large increase in the dispersion of global per capita income. These disagreements are partly because of differences in their models, and partly because of the difficulty of combing national accounts data with household surveys in order to obtain comparable income estimates. New growth theory has also been criticised for its vagueness, unrealistic assumptions (for example, that technology is freely available and useable everywhere), and poor empirical results.

Long-Term Divergence

While mainstream studies remain mired in methodological and empirical difficulties, historical analyses provide an incontrovertible picture of long-term divergence. Five hundred years ago, Asia, Africa and Latin America had 75 per cent of the world's population and a similar percentage of world income. By 1950, their population share had declined to 66 per cent, and their income share had tumbled to 27 per cent. In contrast, the population share of the AEs had risen from 25 per cent to 33 per cent, and their share of world income had reached 73 per cent. These trends were reversed only marginally in the following decades. For example, although the DE share in world gross domestic product (GDP) rose from 15 to 22 per cent between 1970 and 2005, the ratio of the average gross national product (GNP) per capita of the richest quintile of the world's population to the poorest quintile increased from 31:1 in 1965 to 60:1 in 1990, and 74:1 in 1997 (Nayyar, 2009: 2, 6, 13). Similarly, in his careful examination of long-term global growth, Pritchett concludes that:

> Divergence in relative productivity levels and living standards is the dominant feature of modern economic history. In the last century, incomes in the 'less developed' ... countries have fallen far behind those in the 'developed' countries, both proportionately and absolutely.
>
> (Pritchett, 1997: 3, 10)

The observed pattern of global development – at once *uneven* (because it is unequal, with the patterns of inequality changing over time) and *combined* (because countries are economically integrated in multiple ways) – was initially

recognised by Leon Trotsky in the early years of the 20th century. Later work, especially by John Weeks (2001), has identified two levels of uneven and combined development (UCD): *primary UCD* and *secondary UCD*.

Primary UCD derives from the geographically localised emergence of capitalism in Europe and North America between the late middle ages and the 19th century, and the consolidation of manufacturing production in this region. These processes consolidated the division of the world into a small, economically dynamic, highly integrated and militarily aggressive set of 'core' capitalist countries, which set out to dominate a much larger and comparatively slower-changing (in economic terms) set of 'peripheral' regions. In the latter, capitalist relations of exploitation were imposed on top of the pre-existing non-capitalist social relations, leading to complex, but invariably highly exploitative, colonial or semi-colonial relations.

These relationships of international exploitation supported the acceleration of capitalist development in the 'core', and consolidated peculiar social and economic structures in the 'periphery'. While some of these social structures and modalities of exploitation supported the transition to capitalism in the 'periphery', others were inimical to it. As a result of these tensions and the subordinate integration of the 'periphery' into the global economy, primary UCD generates an enduring global pattern of divergence: production, trade, finance and markets expand rapidly among the 'core' economies, while simultaneously the DEs become structurally dependent on 'core' inputs, markets, finance and technology.

Within the 'core' economies, intra-sectoral competition led to rapid productivity growth and the spread of technical advances, simultaneously with the diffusion of new modalities of labour control, while inter-sectoral competition and the expansion of finance supported capital flows that created strong equalising tendencies within and between these economies: 'core' industries and countries tended to move together and grow increasingly similar, in terms of productivity, innovations, institutions and output per capita, forging ahead of the 'periphery'.

Competition within the capitalist areas generates a secondary process of UCD, as it fosters cyclical processes of convergence and divergence across sectors, regions and countries, as new technologies and industries are introduced, expand and eventually decline. These processes are modified by economic and social policies, shifts in income levels, and the mobility and activism of the wage-workers in each economy, which can promote growth or accelerate processes of relative or even absolute decline. Since the ensuing movements of convergence and divergence within capitalist areas are ultimately driven by competition for profits, it is reasonable to assume that they contain a tendency towards convergence, while the counter-tendencies towards divergence are the result of technological lags, sectoral decline, social conflicts and deficient policy implementation.

The interaction between primary and secondary UCD suggests a long-term tendency towards the convergence of capitalist countries and regions, in parallel

with a long-term tendency of divergence between these (capitalist) countries and regions and those areas where social relations are largely, or predominantly, non-capitalist. Examination of the interaction between primary and secondary UCD also suggests that, in periods of rapid accumulation, capitalist countries and regions will tend to converge faster, while in times of crisis they tend to converge more slowly or even to diverge. In contrast, the non-capitalist countries and regions may not converge at all with the 'core', regardless of the speed of global economic growth – unless capitalist relations of production penetrate more deeply in these regions.

Development in the Age of Neoliberalism

The patterns of growth, integration and global convergence have changed recently. After two or more decades of rapid economic growth led by the diffusion of capitalist relations, the expansion of the wage-working class, and the spread of manufacturing, most DEs were heavily penalised by the international debt crisis starting in 1982, and by exceptionally low commodity prices between the mid-1980s and the early 2000s. Under strong pressure from the International Monetary Fund (IMF), the World Bank and the US administration, working in close association with domestic capital and home-grown neoliberal technocrats, dozens of DEs and former socialist economies discarded their developmentalist economic strategies, which tended to stress manufacturing growth, and introduced policies inspired by the Washington (and later post-Washington) consensus.

In many countries, these policies led to one and, sometimes, two 'lost decades' with little if any per capita income growth, rising inequality, deindustrialisation, and the proliferation of precarious forms of employment. These destructive processes have supported the rapid spread of capitalist relations of production and 'core' economic domination around the world. Neoliberal 'adjustment' strategies and 'market-led' policy reforms have supported the expansion of global capitalism into hitherto inaccessible areas of the world, including the former Soviet Bloc, China, India, and vast regions of Asia, sub-Saharan Africa and Latin America.

Dismay with the macro-economic performance of most DEs since the early 1980s was supplanted by a wave of optimism in the mid-1990s, which intensified in the early 2000s as most DEs recovered smoothly from the bursting of the dotcom bubble, and soon achieved annual GDP growth rates around 5 percentage points higher than the AEs (Akyüz, 2012: 10). This process was widely celebrated. For example: 'the world's economic centre of gravity has moved towards the East and South, from OECD members to emerging economies .... This realignment ... represents a structural change of historical significance' (OECD, 2010: 15).

Despite the historical significance of these transformations, commonly held views of global convergence are often supported by questionable data and the

arbitrary extrapolation of recent performance differences, leading to simplistic and often exaggerated expectations of imminent and unproblematic convergence.

First, claims of convergence are generally based on purchasing power parity (PPP$) measures of DE output. Although these estimates can help us compare living standards in different countries, it is the market value of domestic output (measured in current dollars) that determines the contribution of each economy to global supply and demand, and the expansionary and deflationary impulses that it transmits to the rest of the world.

Second, recent DE growth was fuelled by the commodity price bubble in the early and mid-2000s, which in turn was caused by rapid global growth, especially in China, the financialisation of commodity markets, the recovery of Latin America after two decades under the (post-) Washington consensus, the stabilisation of several African countries, and the gigantic US-centred speculative bubble which burst in 2007. These conditions are hardly replicable, much less over several decades.

Third, and despite the hype, claims of global convergence hinge almost entirely on the performance of two countries, China and India.

Fourth, regardless of the achievements of several DEs, the distribution of income remains increasingly unequal both globally and within most countries (UNCTAD, 2012). At all these levels, claims of convergence need a strong dose of realism, as well as clearer analytical underpinnings.

Convergence After the Crisis

With the outbreak of the global crisis, the international economic environment deteriorated rapidly in all areas that had previously supported the expansion of the DEs: net capital flows turned negative, commodity prices tumbled and economic activity contracted rapidly in most AEs, leading to a sharp drop in DE exports.

The policy responses in most AEs were based on state-sponsored financial sector stabilisation, fiscal spending and monetary policy activism. In contrast, DE policies tended to be both more varied and proportionately larger. This was partly because of the more diversified sources of disruption affecting the DEs, and partly because most DEs had sounder macroeconomic, balance of payments and financial positions than the AEs, giving them additional policy space. The fiscal stabilisation package in 15 Asian DEs reached 7.5 per cent of 2008 GDP, almost three times the average level in G7 countries, and China's fiscal response alone reached US$600 billion (13 per cent of GDP). Large stimuli were also introduced in Argentina, Brazil, Korea, Malaysia, Singapore and Thailand (Akyüz, 2012).

These aggressive responses were supported by the rapid recovery of North–South capital flows. This was an unintended consequence of the fiscal and monetary policy relaxation in the AEs, which was meant to support their own banking systems and restore domestic lending. Yet a large part of the resources

created by AE fiscal deficits and central bank asset purchases slipped to more dynamic (and higher interest rate) economies in the South. The rapid recovery of most DEs reinforced the perception of global convergence, and gave credence to the view that the South had 'decoupled': it could now grow faster than the North, and independently of the latter's tribulations.

Despite its superficial plausibility, examination of the decoupling hypothesis reveals significant weaknesses. First, Wälti (2009) assessed business cycle synchronicity between 34 DEs and four groups of AEs, and concluded that it has not declined recently. These results support the view that 'globalisation brings national business cycles closer together' (p. 3), rather than 'decoupling' them. Second, while decoupling (just like the earlier notion of convergence) has drawn support from DE ability to avoid the worst of the global crisis, it subsequently lost credibility as the prolonged AE slowdown eventually exhausted the potential sources of DE growth. Finally, current debates and the trajectory of leading DEs show that decoupling is incompatible with global financial integration. In other words, if the South intends to decouple from the North – in the sense of being able to sustain growth independently of AE cycles, by pursuing appropriate development policies and neutralising external shocks – it must reduce its degree of exposure to global financial flows, and make greater efforts towards regional and South–South integration of production, trade and finance.

In the longer term, as was shown above, it is impossible to restore the growth-promoting conditions of the pre-crisis global economy. Consequently, unless fundamental changes take place in DE policy making and in their global integration, the recent spurt of convergence is likely to exhaust itself, as part of a cyclical pattern of secondary UCD.

The limitations to growth in China are the most significant example, because of the size and importance of the country's economy, and its influence on global commodity demand. Despite its extraordinary economic achievements in the last decades, China suffers from severe under-consumption because of the low share of household income in GDP (that is, extremely low wages) and high precautionary savings (for example, the dismantling of social provision compels families to save in order to meet their health, education and housing needs). Consumption growth lagged GDP growth throughout the 2000s; in the eve of the crisis, private consumption was only 36 per cent of GDP, and it declined further subsequently (in contrast, in AEs consumption often exceeds 70 per cent of GDP). In 2009, investment accounted for 50 per cent of the country's GDP, and for a staggering 80 per cent of China's growth. However, this will inevitably lead to immense overcapacity and a vast problem of non-performing loans.

The global implications of the unavoidable economic shifts in China will be compounded by the conventional adjustment programmes being imposed in several countries simultaneously, most notably in the Eurozone periphery. These programmes compress demand, support the illusion that all countries can export their way to growth, promote global deflation, and foster persistent and regionally uneven regressive patterns of development.

Drivers of Convergence

In addition to the diffusion of capitalist relations around the world, and the neoliberal economic reforms, three other – more concrete – drivers of convergence have been identified in the literature. They deserve closer examination.

Global Trade and Global Production Networks

No area has been as powerfully symbolic of the RoS as international trade. As late as 1990, North–North exchanges still accounted for nearly 60 per cent of global trade, while South–South trade barely reached 8 per cent and the DE share of global exports reached only 23 per cent. In contrast, by 2008 North–North trade had declined to 40 per cent, South–South trade had reached 20 per cent, and the DE export share was 37 per cent (OECD 2010: 71).

The exceptionally rapid growth of DE trade can be attributed to several factors, including faster growth in most DEs than in the AEs, the commodity price boom, and the rapid opening to trade in many DEs, leading to a steep climb in their export-to-GDP and import-to-GDP ratios.

Although impressive, trade growth data can exaggerate DE performance and its potential developmental impact. First, although higher commodity prices lift national income, they do not directly imply economic 'success', except tautologically. Second, while GDP includes only value added domestically, total exports (X) and imports (M) include value added in other countries; consequently, trade growth tends to inflate the X/GDP and M/GDP ratios without any implications for local income or welfare. This effect is especially significant in countries joining transnational production networks, which involve large imports of inputs for domestic processing and the subsequent export of finished goods, largely for consumption in AE markets. Third, trade growth is a poor indicator of development, because trade generally responds to, rather than leads, economic growth.

Beyond the 'Flying Geese' Paradigm

The vertical integration of production in East Asia has been called the 'flying geese' pattern of development (see Chang, Chapter 16 in this book). It has often been suggested that this modality of regional integration could be generalised as a paradigm for North–South interaction, with the Northern AEs as the leading goose bringing along a flock of Southern DEs, bound together by (almost invariably Northern) trade-promoting foreign direct investment (FDI).

Although this scenario is superficially plausible, the combination of historical interpretation and policy prescription underpinning the flying geese paradigm is insufficient at four levels. First, East Asian development has included both tighter integration of production networks within the region and the incorporation of East Asia into the global economy, largely through production for AE

markets. Consequently, the growth of regional trade is due not generally to the flow of final products, but instead to the flow of inputs into increasingly complex transnational production chains for processing for extra-regional consumption. Historically, the movements of capital, technology and manufacturing capacity within the region, and the upward mobility of countries, were predicated on access to AE markets, which may not be available to newer generations of DEs after the crisis.

Second, it is implicitly assumed that transnational corporations (TNCs) are benevolent conveyors of industrial knowledge, that are willing to share their technologies through FDI, licensing, subcontracting, technical assistance and joint projects, that local firms in countries down the chain can absorb these technologies smoothly, and that local firms can expand and diversify their output mix despite the competitive pressures from firms based in more advanced economies. However, this may not be the case, because their competition might instead throttle relatively smaller and undercapitalised firms in the peripheral countries.

The upshot may be a complex pattern of transnational integration with deindustrialisation, which can be understood in terms of secondary UCD. To the extent that manufacturing development takes place in the periphery, it is likely to increase local dependence on imported capital, technologies and components, with limited linkages across local suppliers. This helps to explain why poorer countries entering the East Asian regional division of labour often run trade deficits with Japan, South Korea, Taiwan and China.

Third, instead of being either the outcome or the harbinger of growing cooperation between increasingly autonomous DEs, East Asian integration closely resembles the hierarchical trade and investment relations between North and South.

Fourth, and more prosaically, it is not clear that significant tranches of manufacturing production will move out of China any time soon. Given the country's rapidly improving infrastructure and vast reserves of unskilled labour, manufacturing production is just as likely to migrate within China for many years, drastically reducing the scope for 'flying geese' with other DEs.

In sum, expectations that flying geese provide a realistic depiction of East Asian industrialisation, and that this model can support the convergence of new DE economic blocs, gloss over the analytical and historical shortcomings of the model, and greatly exaggerate its policy relevance. Despite the limitations of this particular model, it remains true that South-centred production networks can diversify the sources of DE growth, expand the scope for DE manufacturing production and open new export markets. This process can be supported by the production of low-tech goods or host assembly operations in poorer DEs, while the more advanced countries provide them with markets, technology, capital, and trade and investment credit. These arrangements can be supported by monetary and financial policy integration and the expansion of regional infrastructure. This would not amount to a BRICS-centred flying geese strategy, because the production networks, markets and sources of capital would be diversified, rather than

being centred in one leading economy; the physical and financial infrastructure should include a range of countries, rather than connecting ever more closely a given hierarchy of countries, and manufacturing development should be closely connected with national industrial policies, rather than simply accommodating TNC strategies.

Industrial Policy and Manufacturing Growth

Historically, the countries that have converged with the 'core' have managed to dislocate binding cost, technological, labour market and balance of payments constraints, through the diffusion of capitalist social relations and the expansion of high-productivity manufacturing activities. As a result of these processes, the DE share in world manufacturing value added (at 1975 prices) increased from 8 to 11 per cent between 1960 and 1980. In the following decade, this share (at 1980 prices) rose only from 14 to 15 per cent, but between 1990 and 2007 this share (at 2000 prices) shot up from 16 to 27 per cent (Nayyar, 2009: 20). It was explained above that overcoming primary UCD is both complex and costly; it is, then, unsurprising that these achievements were concentrated in a small number of countries, especially Brazil, China (including Hong Kong and Taiwan), India, Indonesia, Korea, Malaysia, Mexico, Singapore, South Africa, Thailand and Turkey.

Their achievements depended on rapid capital accumulation, the careful selection of sectoral priorities, technological learning and institutional adaptation, and a conducive financial, institutional and regulatory framework, which can be encapsulated in the notion of industrial policy. These experiences confirm the heterodox economics view that economic growth is sectorally biased: a unit of value added can have a very different impact on long-term growth, depending on the sector where it is produced.

The manufacturing sector plays a key role in rapid growth and development for five reasons. First, manufacturing growth fosters diversification, backward and forward linkages, agglomeration economies and dynamic economies of scale through learning-by-doing. Thus, manufacturing tends to 'pull' the other economic sectors, even when they are initially larger. Second, manufacturing offers greater scope for productivity growth than agriculture or services, especially through the development and adaptation of new technologies. These innovations are subsequently diffused across the economy through the spread of new skills and production methods and the sale of manufactured inputs. Third, manufacturing productivity tends to rise with the rate of growth of manufacturing output, potentially creating virtuous circles of growth across the economy. Fourth, manufacturing fosters export diversification and the production of import substitutes, which can alleviate the balance of payments constraint. Fifth, manufacturing sector wages tend to be relatively high, which can support demand growth and improvements in living standards. Hence, intersectoral shifts of labour and other resources towards manufacturing can help to raise productivity and growth rates

in DEs. Conversely, economic structures narrowly determined by static comparative advantages, as is envisaged by mainstream economics, are sub-optimal for long-term growth and for global convergence.

Successful policies supporting manufacturing sector growth are almost invariably heterodox. Nowhere did markets spontaneously conjure the conditions for long-term manufacturing growth, and economic planning has been extensively used in all converging countries (see Selwyn, Chapter 4 in this book). However, growth for growth's sake is an insufficient economic strategy; the goal of economic development must be the improvement of the living conditions of the vast majority of the population. This type of growth pattern – known as pro-poor growth (Saad-Filho, 2007) – is defined by a faster increase in the incomes of the poor than in the incomes of the rich; in other words, growth is pro-poor when it reduces not only absolute poverty but also relative poverty (that is, the distance between the rich and the poor in terms of income). This is best achieved through a democratic development strategy, which improves the incomes as well as the bargaining position of the workers and the poor, potentially supporting a self-sustaining process of economic, social and political inclusion.

The Way Forward

Convergence is essential for the achievement of a more equal and balanced world economy, and decoupling would help the South to converge. Despite encouraging signs recently, decoupling and convergence remain elusive. Much of the catch-up in the last 30 years is attributable to fast growth in a small number of DEs, and more recently to the impact of high commodity prices; most DEs remain heavily dependent on the AEs, performance disparities within the South continue to be significant, and over the long term, most DEs have underperformed relative to the AEs.

Two more immediate challenges also demand a rethink of DE development strategies. The first is the risk of further global slowdown, which could be triggered by continuing stagnation or another finance-led slump in Western Europe, Japan or the United States. Second, DEs cannot expect the return of the growth pattern they enjoyed during the early 2000s boom, even after an eventual economic recovery in the AEs.

The challenges of stable, rapid and pro-poor economic growth in the DEs can be addressed only through a careful choice of economic policies supporting rapid accumulation and productivity growth, and the coordinated expansion of employment and demand, assisted by greater South-South integration and cooperation initiatives. Convergence and decoupling are important for these countries, and progress towards these goals would facilitate distributional improvements, employment creation and poverty alleviation. Faster progress along these lines is essential, although it remains conditional on unconventional policy choices and improvements in the living conditions of the majority of the population.

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