Rethinking Global Development Policy for the 21st Century

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I am really glad to be with all the people in this room. CGD's work is thinking and doing on the problems and challenges of economic development. And I believe that the development environment is more different today than it probably has been at any moment in the last generation. You can argue that it was an equally different world after the Berlin Wall fell in 1989, I suppose, but there certainly has been no comparable discontinuity since that time.

And that means that the questions we ask must change, and, if the questions we ask change, then it is almost certain that the answers we get and the policies we recommend will change, as well. And so I think the work of CGD is exceptionally important now. That is why I am honored to be the board chair, enormously respectful of the work that was done for many years under Nancy Birdsall's leadership, and look forward with great anticipation to the work that is being done by you, Masood, and by all of your colleagues.

What I want to do tonight is to reflect with you for a little while on just what it is that I think is different and what that says about the development agenda going forward.

I think the place to start and the place to linger a bit—because in all the doom and all the gloom and all the concern we tend to forget it—is that emerging markets have, in a profound sense, emerged over the last generation. There has been more convergence between poor people in poor countries and rich people in rich countries over the last generation than in any generation in human history.

The dramatic way to say it is that between the time of Pericles and London in 1800, standards of living rose about 75 percent in 2,300 years. They called it the Industrial Revolution because for the first time in human history, standards of living were visibly and meaningfully different at the end of a human lifespan than they had been at the beginning of a human lifespan, perhaps 50 percent higher during the Industrial Revolution.

Fifty percent is the growth that has been achieved in a variety of six-year periods in China over the last generation and in many other countries, as well. And so if you look at material standards of living, we have seen more progress for more people and more catching up than ever before. That is not simply about things that are material and things that are reflected in GDP. The primary message of the Global Health 2035 Report that I coauthored several years ago and that Amanda Glassman and others from CGD were involved in was that if current trends continue, with significant effort from the global community, it is reasonable to hope that in 2035 the global child mortality rate will be lower than the US child mortality rate was when my children were born in 1990. That is a staggering human achievement.

It is already the case that in large parts of China, life expectancy is greater than it is in large parts of the United States. One can tell a similar story in terms of literacy and probably an even stronger story of the rights of women. Extreme poverty is now a phenomenon not of countries that just happen to be poor. It is a phenomenon that reflects pockets of poverty in countries that overall have reasonable incomes, like India or China, and it is a phenomenon of fragile and dysfunctional states that do not have effective governments. It is not a phenomenon of generalized poverty of countries that do not lack resources.

And so we have made incredible progress in the last generation. And if we do as well over the next generation, that generation will be one of the two best generations in human history in terms of poverty reduction. And so as we move to a discussion of how dark it is and populism in industrial countries and all the things I am about to talk about, we should not lose sight of that hugely positive reality, which will be the primary thing that historians who look at this time in terms of these questions in 2300 see.

The second thing I want to say in terms of how the world is right now is a more painful and more difficult thing. And that is that the alignment of interest between the United States and the developing world as perceived by Americans is greatly diminished from where it was a generation ago. That is for two broad reasons. In part, it is because we are no longer engaged in the Cold War and the associated struggle for allegiance and the associated idea that if developing countries succeeded with our capitalist market system then they will be on our side, not their side, and therefore we had a huge stake in their success because we were involved in a global struggle, they were our allies, and we needed them to succeed.

There is no parallel global struggle of the same kind today. Therefore, the kind of idea—and if you think about it, it is actually quite a remarkable idea—John Kennedy, speaking albeit more about the military dimension than about the economic dimension, said, with respect to developing countries, we will "bear any burden and pay any price to ensure the success of liberty." And then he paused and he said, "All of this and more."

Now, Vietnam had something to do with why we moved away from that. But the fact that there is no existential struggle that has children practicing drills hiding under their desks has something to do with a very different attitude towards development.

The second difference that is related—the second reason for this misalignment is a consequence of the very success that I just described. There was no economic threat that was important to the United States from the developing world a generation ago. Yes, if you were a textile worker, you were worried about imported shirts. Yes, if you were a shoemaker, you were worried about imported shoes. But for the most part, there was very little that was happening in the developing world that was a competitive challenge to substantial-sized interests in the United States.

That is not a plausible assertion today. I believe there is a great confusion in the economic policy discussion. The truth is that trade has had substantial effects on the American income distribution and substantial effects on large numbers of American workers. The untruth is that trade agreements have had substantial impacts on American workers and the American income distribution.

The reality is that the American market has been almost completely open for 40 years. And what has happened is that the developing countries have become much more productive and much more efficient and it has become much more possible to move goods at low cost and to export efficient production technologies to developing countries, and that would have happened with or without trade agreements, and the trade agreements have been good deals because they have opened the other countries' markets much more than they have opened ours, mostly because ours was already open.

But the consequence is that economic interests are much less aligned than they previously were. Moreover, China represents an extraordinary and, in many ways, unprecedented situation. It is, I believe, without historical precedent for the world's largest economy to have average standards of living that are 25 percent of the world's frontier—high frontier in terms of standards of living. And it is, I believe, without precedent for a country with 25 percent of frontier standards of living to have a range of global companies that are at or beyond the cutting edge in key technologies.

Take two examples. On Alipay, there is a range of views. There would be those who would say that Alipay is three years ahead of PayPal and American fintech, and there would be those who would say that it was 10 years ahead of American fintech. There would be no one knowledgeable who would say that in a range of spheres Alipay is not ahead of American fintech.

And if you think about the phrase "fintech," those are two things that we think of the United States as being extraordinary good at. A similar case can be made for other parts of Alibaba, for WeChat, and for a range of other Chinese companies.

And so the idea that the success of the developing world is an obvious positive objective of US economic policy is not as readily apparent to the current generation as it was to previous generations, and that is not an entirely irrational feeling on their part.

The third framing reality that I want you to think about is that our money—and I mean by that our assistance and the assistance of the multilateral institutions in which we have great leverage—is much less significant than it once was. Perhaps the best way to convey that is with a story.

In 1991, when I was new to all of this, I was working as the chief economist of the World Bank, and the first really important situation in which I had any visibility at all was the Indian financial crisis that took place in the summer of 1991. And at that point, India was near the brink. It was so near the brink that, at least as I recall the story, $1 billion of gold was with great secrecy put on a ship by the Indians to be transported to London, where it could be collateral for an emergency loan that would permit the Indian government to meet its payroll at the end of the month.

And at that moment, the World Bank was in a position over the next year to lend India $3 billion in conjunction with its economic reform program. And the United States had an important role in shaping the World Bank's strategy. Well, that $3 billion was hugely important to the destiny of a sixth of humanity.

Today, the World Bank would have the capacity to lend India in a year $6 billion or $7 billion. But India has $380 billion—$380 billion—in reserves dominantly invested in Treasury bills earning 1 percent. And India itself has a foreign aid budget of $5 billion or $6 billion. And so the relevance of the kind of flows that we are in a position to provide officially to major countries is simply not what it once was.

Now, in many ways, that is a reflection of the success I described earlier. If India had not converged substantially, if emerging markets had not emerged, they would not have anything like those quantities of reserves. But the reality is that realities that frame thinking about economic development, then, are it is working for most emerging markets. The idea that simply making it work—the idea that people should be taxed heavily to make it work better is a much less intuitive idea politically for deep reasons in the current context that it ever was before, and the capacity for marginal money to make a major difference in major places is vastly less than it ever was before.

And I would suggest that it is that thinking that needs to inform our thinking about development going forward. What would be principles that need to be very important for us in thinking about development going forward? I would suggest five.

First, providing money for tasks that governments are already carrying on, on a significant scale, is unlikely to be enormously impactful. In part, that is a matter of the arithmetic that I just described. In part, that is a matter of the unspoken word in much of development economics, which is fungibility.

I remember as a young economist who was going to be the chief economist of the World Bank sitting and talking with Stan Fischer, who was my predecessor as the chief economist of the World Bank. And we were talking, and I was new to all this. I had never done anything in the official sector. And I said, "Stan, I don't get it. If a country has five infrastructure projects and the World Bank can fund two of them, and the World Bank is going to cost-benefit analyze and the World Bank is going to do all its stuff, I would assume what the country does is show the World Bank its two best infrastructure projects, because that will be easiest, and if it gets money from the World Bank, then it does one more project, but what the World Bank is actually buying is not the project it is being shown, it is the marginal product that it is enabling. And so why do we make such a fuss of evaluating the particular quality of our projects?"

And Stan listened to me. And he looked at me. He's a very wise man. And he said, "Larry, you know, it is really interesting. When I first got to the bank, I always asked questions like that."

"But now I've been here for two years, and I don't ask questions like that. I just kind of think about the projects, because it is kind of too hard and too painful to ask questions like that."

Well, the story is a little unfair to me, and it is a little unfair to Stan, and it is a little unfair to various things the Bank does, and it is the reason it gets involved in sectors. But it still captures a deep truth that we tend not to face when we think about what it is that we are financing.

So we have one other way to make this point, which I was kind of struck by when I taught my class on globalization this semester. I gave a lecture on the Marshall Plan—the great historical success of foreign aid. And if you Google the words "Marshall Plan," you can find calls within the last two years for 12 different Marshall Plans. A Marshall Plan for America's cities, a Marshall Plan for Appalachia, a Marshall Plan for Africa, a Marshall Plan for Puerto Rico. Everybody who wants to help someplace calls for a Marshall Plan for that place, because the Marshall Plan is the great positive, inspiring feature of foreign aid.

Well, here's the remarkable fact that I had not appreciated. The Marshall Plan lasted four years, and during those four years, it represented about 4 percent of the GDP of the countries that were receiving assistance. Now, there are several dozen countries this year that are receiving more than 4 percent of GDP in assistance and have received more than 4 percent of GDP in assistance for a decade.

Take a troubled area, an area that is recovering from conflict, an area that needs to be reconstructed, like Europe did after World War II. Take Bosnia in the decade after the struggles there, or take parts of the Middle East. Take a standard World Bank needs assessment—there is been a civil war in a country and the civil war has settled; we are there is going to be a donors conference and the World Bank convenes to prepare a needs assessment. I can save you the trouble—the needs assessment will be between one-third of GDP and one-half of GDP for the affected region for five years per year. Ten times the Marshall Plan.

Now, what that reflects is that the Marshall Plan was actually a different context—that reconstruction is very different from development. But the message that you can simply solve the problems by moving fungible money in is probably not realistic. And so I would say the first lesson is that we need to think in increasingly different ways than traditional mobilize more money for foreign assistance.

And the first bit of advice I gave Masood as he was thinking about his agenda was that the largest share of CGD reports has to not be a new rationale for more foreign aid to countries about a given objective without any change in existing foreign aid.

The second reality is that this is not a rationale for less development spending. This is a rationale for the same amount of development spending that we have, or for more development spending, because there is a different agenda—an agenda where fungibility is much less of a problem and an agenda where the returns are probably even higher, and that is the sphere of global public goods.

The level of investment in new agricultural technologies, the level of investment in developing responses to the next pandemic—and, by the way, it is at least even money that sometime in this century there will be something comparable to the 1919 flu epidemic that killed two-and-a-half times many people as World War I. And if that comes, it is an open question whether the fact that we have modern science will help us more than the fact that we have modern intercommunication between places hurts us. And the current WHO budget for pandemic flu is less than the salary of the University of Michigan's football coach—not to mention any number of people who work in hedge funds.

And that seems manifestly inappropriate. And we do not yet have any settled consensus on how we are going to deal with global public goods and how that is going to be funded. We have the sentence that I and many others have uttered many times, that “global development banks need to shift their focus increasingly to global public goods.” Good sentence. Really good sentence.

There is a problem, which is that when you lend money to India, especially when you lend money to India when it has its $380 billion of reserves, then whether the project works or whether the project does not exactly work, India is probably going to pay you back. But when you invest money in hiring a bunch of scientists to develop a standby capacity to deal with the next pandemic, there is no pecuniary source of revenue to pay you back, and it is much more expensive to spend money than it is to lend money to the relative creditworthy.

And we have not achieved any meaningful consensus on large-scale commitments to funding of global public goods by the major countries. It was treated as a great achievement at one of the summits. And in its way, it was a great achievement when the countries of the world all organized themselves to spend $100 million or so buying a $500 million policy of insurance, reinsurance that would address pandemics. Well, against any pandemic of any size, $500 million is roughly nothing. And this was the big outcome from the heads of state of the world coming together to show that they could deal with global public goods.

How we are going to mobilize support around global public goods, where the resources are going to be adequate around global public goods, I would suggest, is the second very large priority for the years ahead.

Third is the management of global private sector integration. And I choose those words quite carefully. We have these agreements that we call trade agreements, that we call free trade agreements, and that we associate with the greats of economics, like David Ricardo and Anne Krueger, who have made the case through many years, and made a compelling and persuasive case for free trade. And they are, with some exceptions that the economics profession understands and that for most purposes are not hugely important. Theirs is an overwhelming case that erecting tariff or quota barriers to trade between countries is usually a bad idea.

Most of those tariffs in today's world have gone away. And most of the content of what we now call free trade agreements beyond where we are now is not about the removal of those kinds of barriers. It is about, for example, securing intellectual property protection for global companies in a wider range of countries. Or it is about achieving access for service companies to a wider range of countries. Or it is about harmonizing rules in areas like safety standards or financial reporting standards.

All of those things may be good or they may be bad, but they are not self-evidently and clearly good in the way that free trade is clearly good. And part of the reason there is a sense that there is a bit of a swindle going on is that the prestige of free trade is being arrogated in support of a rather different agenda of better, more harmonized commercial rules with a sense that the participants in the debate about what constitute better, more harmonized commercial rules are mostly the kinds of people who appear in Davos rather than the kinds of people who work in the companies that are run by the people who appear in Davos. And there is a suspicion of that agenda.

Let's take a different issue. It is an issue that is mentioned in international economic dialogue, but not with nearly the emphasis, prestige, or political attention that is assigned to so-called free trade issues. And that is the set of issues pointed up by the Paradise Papers or the Panama Papers, the substantial avoidance or evasion—choose your preferred word—it is fine if you choose whichever one you think of as the lesser sin—that takes place.

There is no reason why preventing a race to the bottom in the taxation of mobile capital should not be an equally important priority for those concerned with international integration as the dissemination of intellectual property protection or the protection of investors' rights or the establishment of the right to branch. And that is an issue that—because revenues not obtained in one place have to be obtained in another place—speaks very directly to the economic interests of broad publics everywhere.

So I would describe as a third priority, without knowing exactly how it is done, the recasting of the current debates about free trade, which really are not about free trade, as debates about the management of international economic harmonization to the benefit of middle-class people everywhere.

The fourth issue that I would highlight—and I can highlight its importance more credibly than I can speak intelligently about it—is addressing the set of issues having to do with the movement of peoples. It is on the one hand the case—and it is the point that economists emphasize—that if you think about the size of the barrier represented by the difference between the price of a car here and the price of a car there, or the price of a shirt here and the price of a shirt there, and you look at that barrier as a percentage, or you look at the cost of money here and the cost of money there, you look at that as a percentage or you measure the barrier, and then you look at the wage rate for an equivalent worker in one place and in another place, the barrier, the imperfection relative to full mobility and full openness is an order of magnitude greater with respect to the movement of people than it is with respect to the movement of capital or the movement of goods. And that is the globalist pure economic case for much freer movement of people than we have today.

At the same time, there is the tension represented by the fact that while it might be difficult for moral philosophers to fully justify and understand, most of us care more about our children than our nephews, and most of us care more about our nephews than we care about our friends' children, and most of us care more about our friends' children than we care about strangers' children, and most of us care more about other American children than we care about children in other countries.

And so an agenda of collective globalization is an agenda that is intentioned with bringing out the most generous impulses within us. And how we manage that tension is, I think, central going forward. I would like to see a world in which there is more movement of peoples, a world in which there are more opportunities for us to prosper and for developing countries to prosper, through more mobility, temporary or permanent, of peoples. I find the CGD work pointing up the magnitude of those barriers to be highly persuasive.

But at the same time, if the consequence of that is a backlash against generosity and a turn towards a hyper-truculent nationalism, it is not going to work. And so I don't know what the solution is. But I do not think there is a more important development issue than getting questions of migration right, especially in a world where the growth rate of the industrial world's labor force over the next 40 years is going to be zero, and where that reality will not be changed—and indeed, will be exacerbated—if we think of China as entering the industrial world over those 40 years.

And the last challenge is how are we going to shape a world in which China is going to loom ever larger. The sums of money that appear to be on the offing around One Belt, One Road dwarf the kinds of sums of money that we talk about when we talk about new US assistance initiatives, or even when we talk about new World Bank initiatives or, frankly, when we talk about the entire lending budget of the World Bank.

Right now, I would describe the modus vivendi that the world has found as being parallel play. The West does its thing; China does its thing. Countries get a bunch of money from China and they do it China's way. Countries get a bunch of money from us and they do it our way. And we all sort of move forward together and periodically we have some dialogue with China about how this system is going to work, and everybody is very polite to everybody else.

I'm not sure that that is going to work when nobody is alive who remembers the tradition of Bretton Woods and when China's GDP is 75 percent greater than the US GDP. And so the last challenge I would say is, what is the system of global governance in which the United States and the West and China are all going to participate in, in common?

I have by now had a chance to be part of any number of groups of Americans discussing strategy towards particular regions or strategy towards particular countries. And what I have noticed is that there is a strong tendency for people, it seems to me, to confuse a strategy with a wish list. Our strategy is that it is very important that they open their markets, that it is very important that they cooperate with us on this security issue, that it is very important that they have a better attitude towards our companies that are investing in their country, and other things.

Well, that is a good wish list. But a wish list is not a strategy. A strategy needs to be something that is feasible, and probably their deciding to adopt our wish list because we say our wish list louder and more firmly does not constitute a strategy. And I do not think we as yet have a strategy for thinking about the management of the global economic system that is appropriately respectful of the scale and achievements of the Chinese economy.

So I want to end where I started, by saying that with all the challenges that are ahead, if we keep the development trend of the last generation going substantially, even if not completely, we will do very well. But the keeping it going will require a great deal of new thinking that is not primarily going to be about giving foreign aid to countries. Instead it is going to be about mobilizing countries around global common interests on significant scale, around managing global economic integration in a way that is in the interests of all citizens, that thinks about the movement of peoples differently in a world that technology is making far smaller, and that engages in a much more serious way with China on questions of global economic policy than we have so far.

Thank you very much.