

## Summing Up Structuralist Development Macroeconomics and New Developmentalism

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*The author argues that the economic development model that has prevailed since the 1970s is outdated, if not outright wrong. He proposes a more compelling one that has a prominent place for wages and demand, structural and institutional influences, and exchange rate management. The question, then, is how to get this message heard.*

**I**N THE PAST TEN YEARS, a group of Keynesian and structuralist economists have been developing a *structuralist development macroeconomics*—that is, a theory based on the macroeconomic assumption that the development bottleneck lies in the shortage of demand or

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of lucrative investment opportunities rather than in supply-side factors, on the one hand, and on a structural conception of economic development and on structural tendencies that repress demand, on the other hand. Whereas the tendency of wages to grow more slowly than productivity limits internal demand, the tendency to the cyclical overvaluation of the exchange rate makes the international market inaccessible to enterprises in developing countries, including those that use worldwide state-of-the-art technology.

These same economists, taking into account structuralist development macroeconomics and the current experience of the dynamic Asian countries, have been developing a national development strategy or a strategy of international competition—*new developmentalism*—which they present as an alternative to the Washington Consensus or the conventional orthodoxy, an alternative that makes macroeconomic policy more responsible than the conventional orthodoxy and more likely to promote economic growth with stability and equity. Some of these economists gathered in São Paulo in April 2010 and drafted “Ten Theses on New Developmentalism” as an alternative to the Washington Consensus. The theses were subjected to a wide-ranging discussion, and in September 2010, eighty distinguished development economists subscribed to them.<sup>1</sup> These new ideas and policies apply mainly to middle-income countries, but I believe that they are useful for developing countries as well.

These ideas can be considered a second moment of the structuralist development economics that a pioneering group of development economists elaborated between the 1940s and the 1960s.<sup>2</sup> Structuralist development economics, which combined elements of classical political economy with Keynesian macroeconomics, was the mainstream in the 1950s and 1960s but experienced a crisis in the 1970s. During the 1980s and the 1990s, neoclassical economics and neoliberal policies and reforms became dominant. We lived in the time of the “single way.” But since the early 2000s, the ideological character of neoclassical economics and the failure of neoliberal policy prescriptions have become obvious. The developing countries that adopted these policies did not experience financial stability, growth, or a reduction in inequality. On

the contrary, the policies benefited only a minority of the population, while some Asian countries that rejected most of them, like China and India, enjoyed growth and financial stability.

Accordingly, since the early 2000s development economics has been reviewed and updated in several developing countries, particularly Brazil, leading to the emergence of new developmentalism. When the global financial crisis broke in 2008, the failure of neoclassical economics became obvious in the rich countries, which fostered the renewal of development economics. The outcome was a set of new theories, centering mainly on financial globalization and the exchange rate and constituting what we call “structuralist development macroeconomics.” It was, clearly, a second moment for development economics, this time emphasizing the demand side and access to international markets.

Economics textbooks deal separately with macroeconomics and economic development, on the assumption that the study of short-term problems and of the stability of economic systems would be the object of macroeconomics, and the long-term process of economic growth the object of development macroeconomics. I aim to integrate these two perspectives in structuralist development macroeconomics. After all, development’s long term is the sum of macroeconomics’ short terms, and the existence of demand is the key variable in the determination of investment. When we study economic development on the supply side, we usually think in terms of deficiencies or “lacks”: lack of capital, lack of basic education, lack of top-level technical and administrative knowledge, lack of planning to develop the infrastructure and basic industries, lack of good institutions and well-functioning markets to coordinate competitive industries and foster investment. The supply side is obviously important in economic development, but there are no new ideas in this area, and each country tries to do its best in this matter. As well, economic research usually demonstrates that the fundamental variable that explains different rates of growth is not on the supply side but is the ratio of investment to the gross domestic product (GDP). The higher the rate of capital accumulation, the higher a country’s growth rate, and this rate is a function of profit expectations, which, in turn, are a function of the aggregate domestic demand for goods and services

and of the access that national firms using competent technology have to foreign markets. This depends mainly on two key macroeconomic prices: the interest rate and the exchange rate.

Therefore, it is not reasonable to separate macroeconomics from the theory of economic development. It is more reasonable to combine them under the denomination of “development macroeconomics.” But, because I take a structuralist view of economic development, I believe that the “structuralist” complement is adequate. Structuralist development macroeconomics may be *defined* as the economic theory that explains economic development as a historical process of capital accumulation with the incorporation of technological progress and structural change and depends on the existence of domestic demand and an exchange rate that guarantees profitable investment opportunities to business enterprises using state-of-the-art technology. It is the theory that affirms that the growth rate is a function of profit expectations, which are a function of internal demand and of the access of the country’s enterprises to external demand. It is the theory that regards the increase in wages and the growth of the domestic market as a long-term strategy and as the aim of economic development, but, in order to accelerate growth, adopts for a period an export-led strategy that allows developing countries to make use of their cheaper workforces in order to grow. It is the theory that identifies in the developing countries two structural obstacles on the demand side: the tendency of wages to grow more slowly than productivity, limiting domestic demand, and the tendency to the cyclical overvaluation of the exchange rate, limiting the access of national business enterprises to world markets.

The set of ideas that I sum up here is part of a broader and ongoing process of revising development economics that was originally elaborated in many papers and in *Globalization and Competition*.<sup>3</sup> The revision of economic theory and policy making became imperative for economists in the developing countries in view of the success of the dynamic Asian countries that did not accept the propositions of the Washington Consensus; subsequently, after the global financial crisis of 2008, that revision also became necessary for rich countries, insofar as the policies that they recommended to developing coun-

tries proved equally bad for themselves. Here I make a synthesis of the chief concepts and models of structuralist development macroeconomics and a brief comparison between new developmentalism and the Washington Consensus. It is important to point out that new developmentalism will in practice need to be constantly reviewed and that structuralist development macroeconomics is a work in progress, open to new developments and to empirical tests.

## **The Exchange Rate at the Center of Growth Theory**

The central assumption of structuralist development macroeconomics is that the economic system is formed by four primary agents: entrepreneurs who make profits; rentier capitalists who receive interests, rents, and dividends; workers who are paid wages; and professionals who receive salaries. The main condition for the realization of investment and savings is a satisfactory profit rate. At the same time, wages and salaries, whose increase is ultimately the justification of economic development, should grow along with the increase of productivity, so that if the expected profit rate is satisfactory, it remains so. Finally, it is necessary that capitalist rents be as low as possible, because capital is relatively abundant in modern economies, and because the higher rents are, the lower are profits, wages, and salaries—the returns to the people who actually generate growth. Rentier capitalists associated with financial professionals and legitimized by neoclassical economics fight to achieve and justify high rents, which they generate from financial speculation, derivatives, and other “financial innovations.” In relation to the interests of rentier capitalists, the big problem faced by the rich countries is the excessive share of rents in GDP, whereas the big problems for the developing countries are high domestic interest rates and an overvalued exchange rate, which constrain lucrative investment opportunities.

Although economic growth also depends on factors on the supply side (education, technical and scientific progress, investment in infrastructure, good institutions), structuralist development macroeconomics claims that the obstacles to it lie rather on the *demand* side. Economic development depends on a high investment rate, which

depends not on high prior savings but on the existence of lucrative investment opportunities for companies, which in turn depends on the existence of domestic demand and access to foreign demand. But in developing countries, two *structural tendencies* depress demand: the tendency of wages to grow more slowly than productivity, which holds down domestic demand, and the tendency to cyclical overvaluation of the exchange rate, which puts foreign demand out of the reach even of efficient domestic companies.

The first tendency results from the existence of an unlimited labor supply in developing countries. The major advantage of those countries vis-à-vis rich countries lies in their cheap labor, but, since it is abundant, it tends to be poorly remunerated, which raises the problem of a weak domestic market. As Celso Furtado stressed, development policies should always be concerned with this problem, not only for the sake of social justice, but because sound and sustained growth is not compatible with stagnant wages. This tendency fades away as economic development takes place and real wages increase. When the country reaches the “Lewis point”—the point at which the unlimited labor supply disappears—wages tend to grow nearly as fast as productivity, and the tendency ceases to hold.

The second tendency—the tendency to the cyclical overvaluation of the exchange rate—is new in the economic literature. Due to it and because the exchange rate tends to be chronically overvalued—to be overvalued in the long term—the exchange rate lies at the core of development economics. Neoclassical economics and Keynesian macroeconomics fail to detect the tendency because for neoclassical economics, the exchange rate floats gently around the current equilibrium, while for Keynesian macroeconomics, the exchange rate exhibits high volatility but always around the current equilibrium: In other words, both approaches assume that exchange rate “misalignments” are limited to the short run. In contrast, structuralist development macroeconomics sees the exchange rate as being cyclically and chronically overvalued, and it offers three explanations: the critique of growth with foreign savings, the model of the Dutch disease, and the model that explains why developing countries lurch from sudden

stop to sudden stop, from currency crisis to currency crisis, when their exchange rate is not duly managed and this tendency neutralized. Therefore, the equilibrium price for the exchange rate is not just a macroeconomic problem; it is also a major growth problem.

An overvalued exchange rate is a major obstacle to growth because local firms using international state-of-the-art technology have no access to foreign demand. Thus the exchange rate plays the role of a light switch that turns global demand on or off for technologically competent enterprises. This metaphor may involve an overstatement—it would be more appropriate to think in terms of a gradual progression rather than a cut-off, and so of a dimmer rather than a switch—but it strongly illustrates the damage that an overvalued currency does to competent business enterprises.

Thus, according to structuralist development macroeconomics, the exchange rate in developing countries is regulated not by the market but by cyclical crises of the balance of payments. The cycle begins with a balance-of-payments crisis, that is, with a sudden stop to the refinancing of foreign debt, and an ensuing strong depreciation of the local currency. After the inevitable adjustment that the country is forced to undertake, the exchange rate once again gradually appreciates, in response to the Dutch disease and to capital inflows destined to finance the current account deficit that conventional economics judges “necessary” for economic growth and which developing countries genuinely believe to be so. As a result, the foreign debt rises again, and after some time, creditors begin to lose confidence. When they finally suspend the renewal of their loans in the foreign currency, a new balance-of-payment crisis occurs, and the domestic currency again devalues abruptly and sharply.

This tendency has two causes: the Dutch disease, which affects almost all developing countries, and excessive capital inflows.

## **The Dutch Disease Model**

The Dutch disease is the permanent overappreciation of the exchange rate resulting from the exploitation of abundant and cheap natural

resources (or of cheap manpower coupled with a difference between salaries and wages) and the production of commodities (or of low value-added per capita manufactured goods) that can be exported at a considerably higher exchange rate than is required to make other business enterprises using state-of-the art technology competitive. Thus, the Dutch disease is caused by Ricardian rents and implies two exchange-rate equilibriums: the current equilibrium, which balances intertemporally the current account of the country, and the industrial equilibrium, which makes competent business enterprises internationally competitive.

The difference between these two rates indicates the severity of the Dutch disease. In countries where Ricardian rents are very high and the severity of the disease is high, investment in other industries in the tradable sector will be completely impossible if the country does not neutralize the Dutch disease. This is the case with oil-exporting countries like Venezuela and Saudi Arabia. In other countries, where Ricardian rents are not so high, the difference between the two equilibrium rates is relatively small, and industrialization has occurred because, although the economic authorities did not know about the Dutch disease, they had an intuition of it, and were able to partially neutralize it through import tariffs and export subsidies or through multiple exchange rates. This happened in, for example, Brazil, Mexico, and India.

These are awkward ways to neutralize the Dutch disease. The correct way is the one that Norway has always adopted in relation to oil and that Argentina has adopted since 2002 in relation to soybeans, wheat, and meat. It is to impose a tax on the commodity exports corresponding to the difference between the industrial and the current exchange-rate equilibrium. In consequence, the supply curve of the commodity in relation to the exchange rate (not in relation to the commodity price that is constant in the model) will shift to the left, so that the producers of the commodity will be ready to supply the same quantity only when the equilibrium exchange rate moves from the current to the industrial equilibrium. At the moment this change materializes, the country will necessarily present a current account



surplus. A simple example usefully demonstrates this. Imagine a soybean-exporting country. In this country, the industrial equilibrium exchange rate is 3.00 units of the local currency per dollar, and the current equilibrium exchange rate is 2.00 per dollar. If the government imposes a tax of 1.00 per dollar on the soybean exports, soybean producers will continue to offer the same quantity only if the equilibrium exchange rate changes from 2.00 to 3.00. A freely operating market will take care of this movement of the exchange rate, but, as there is a period of transition, the government will be expected to manage it so as to avoid losses for the producers. In the end, it is not the soybean producer who pays the tax; he remains in precisely the same position, with the same profitability. The country's population as a whole pays the tax, because the consequent depreciation of the currency will cause the prices of tradable goods to rise and real wages to fall. But, subsequently, the economy begins to grow quickly, and this loss will soon be recovered.

What should the government do with the tax revenue? In principle, it should follow Norway's example. Instead of spending it, it should invest it in a sovereign fund. On the assumption that the state budget, disregarding the tax, is balanced, the export tax will constitute a public surplus. If, more realistically, we presume that it is reasonable for countries that do not suffer from the Dutch disease to incur a moderate public deficit (which keeps the country's public debt constant in relation to GDP), in countries that have neutralized the Dutch disease through an export tax the corresponding revenues should result in a budget surplus. If the state decides to spend the tax revenues, it must do so moderately so as to keep the budget in balance.

## **Capital Inflows and Foreign Savings**

Excessive capital inflows in the developing countries are the second cause of the tendency to the cyclical overvaluation of the exchange rate, whose main cause is the "foreign savings fetish"—the belief that those countries "need" foreign capital in order to grow. This belief is expressed in the assumption that developing countries suffer from a

structural shortfall of foreign reserves or a “foreign constraint” that can be overcome by foreign finance in the form of loans and direct investments. The three main consequences or moments of excessive capital inflows are, successively, the substitution of foreign savings for domestic savings, “foreign financial fragility” (which keeps the country often on the brink of a currency crisis), and, finally, a new balance-of-payments crisis. Thus, capital inflows are “excessive” insofar as they do not contribute to economic growth but, on the contrary, contribute to increased consumption, a small or even zero increase in the investment rate, financial dependency, and currency crisis.

In line with the foreign constraint assumption and the policy of growth with foreign savings, developing countries should incur current account deficits and finance them with capital inflows “in order to increase total savings.” To maximize such inflows, they are supposed to keep the domestic interest rate at a relatively high level—a level that “attracts” foreign capital and that checks “financial regression” (low or negative interest rates). Therefore, the search for foreign financing is presented as a good thing in itself, with the deliberate embrace of current account deficits (which, in the economic literature, are designated by the euphemism “foreign savings”) in order to increase the country’s savings rate and, therefore, its investment rate.

This idea is not simply a key one for conventional economics; Keynesian and structuralist economists also believe or believed in it. The two-gap model holds that the “external constraint” is a fundamental limitation because the income elasticity of imports is higher than the income elasticity of exports of developing countries. From these two considerations, the proponents of the foreign constraint infer that the solution is to resort to foreign finance, instead of considering that moving the exchange rate to the industrial equilibrium is a better way of solving the problem. They assume that foreign savings are added to domestic savings, and for that reason they have no difficulty in accepting the existence of a foreign constraint.

Structuralist development macroeconomics denies the existence of an external constraint to be overcome by the policy of growth with foreign savings, insofar as it argues that a large proportion of foreign

savings does not increase the investment capacity of the country but finances consumption and creates long-term liabilities for the country. Rather than adding to domestic savings, foreign savings largely substitute for domestic savings. This happens because the resulting capital inflows cause the local currency to appreciate, which (on the income side) artificially increases wages and consumption (given the existence of a high marginal propensity to consume among the workers) and reduces domestic savings, with the result that foreign savings replace domestic savings rather than adding to them. On the demand side, the appreciation of the domestic currency for a brief period encourages investment, because imported equipment becomes cheaper and because internal demand rises as wages are increased. Yet the picture changes quickly and permanently: local business enterprises cease to be able to export and, worse, begin to be driven out of the domestic market by importers. Efficient business enterprises are disconnected from the global market, the opportunities for export-oriented investments disappear, export-oriented investment declines, the country ceases to take advantage of relatively cheap labor in order to export and catch up, investment falls, and, in Keynesian terms, domestic savings also fall, displaced by foreign savings. The result, according either to the first reasoning (on the supply side) or to the second reasoning (on the income side), is little or no increase in the country's rate of investment and a substantial increase in the country's financial fragility and in the liabilities to be honored through profit and interest remittances. Only in exceptional circumstances, when the country is already growing fast and the marginal propensity to consume is declining, will a policy of growth with foreign savings be beneficial. Usually foreign savings substitute for domestic savings, even if they assume the form of direct investment implying the formation of fixed capital.

This critique of the growth with foreign savings policy may seem strange, but all scientific knowledge implies criticism of intuition. Before Copernicus it was "obvious" that the Earth was flat; before Darwin it was "obvious" that man was created by God in His image and likeness; before Keynes, it was "obvious" that in order to increase

investment, it was necessary first to increase savings. Until now it has also seemed “obvious” that foreign savings would be added to domestic savings and increase total savings, but, besides the economic arguments that I have just presented, there is empirical evidence showing that capital is made at home: a country rarely grows with foreign savings, and, when it does, it does not do so for long. At present the dynamic Asian countries are growing with foreign “dissavings,” that is, with current account surpluses. When four of them (Thailand, South Korea, Indonesia, and Malaysia) forgot this rule and tried to grow with foreign indebtedness, they were engulfed by the 1997 Asian currency crises and immediately changed policy.

There is an additional argument in relation to foreign direct investment. While among developed countries the capture of domestic markets that it implies is mutually compensated insofar as they make and receive direct investment in a reasonably equal amount, this is not the case with developing countries. The reciprocity that exists among rich countries does not apply to them, because they do not host multinational enterprises that can perform the job. Thus, the capital inflows associated with direct investment not only cause the substitution of foreign for domestic savings; they also imply the opening of domestic markets to multinationals without reciprocity. But this does not mean that foreign direct investment is always damaging to developing countries. It is not when it introduces technology or when it creates opportunities for increased exports. This is the case with China, which for many years has achieved a current account surplus, and accepts foreign capital inflow provided it introduces technology or contributes to exports.

The rejection of foreign financing by structuralist development macroeconomics does not mean that finance is not essential to growth. A well-developed national financial system is fundamental to it, as Schumpeter and Keynes so well demonstrated, although in different terms. Its role is to finance investment and, thus, make possible innovation and an increase in savings. The enormous difference between foreign and domestic finance is that the former consists of foreign money, the latter of national money. The state can create domestic

money and, when required, devalue it. A state never goes bankrupt when it is indebted in its own currency. Its sovereignty is preserved. This is not the case with foreign finance. Foreign finance appreciates the national currency and threatens the country with balance-of-payments crises.

The policy of growth with foreign savings is not the only cause of the cyclical tendency to the appreciation of the exchange rate—which explains the continuous appreciation of the local currency after it reaches the current equilibrium and plunges into current account deficit. A second cause is the abuse of the exchange rate as a nominal anchor to control inflation. This is a widespread practice, not only among populist governments but also among central bankers committed to meeting some agreed-to inflation target.

A third cause is “exchange rate populism.” Economic populism is the practice of some governments of spending irresponsibly more than they collect in revenue, aiming at the reelection of their incumbents. Usually this applies only to the state organization, implies budget deficits, and may be called “fiscal populism.” Yet not the state or the government but the nation-state, the whole country, may spend irresponsibly more than it collects in revenue, and incur current account deficits; in this case, we have exchange-rate populism. The twin-deficit theory, which is true when the external accounts of the private sector are reasonably balanced, expresses the interrelationships between the two deficits or the two populisms.

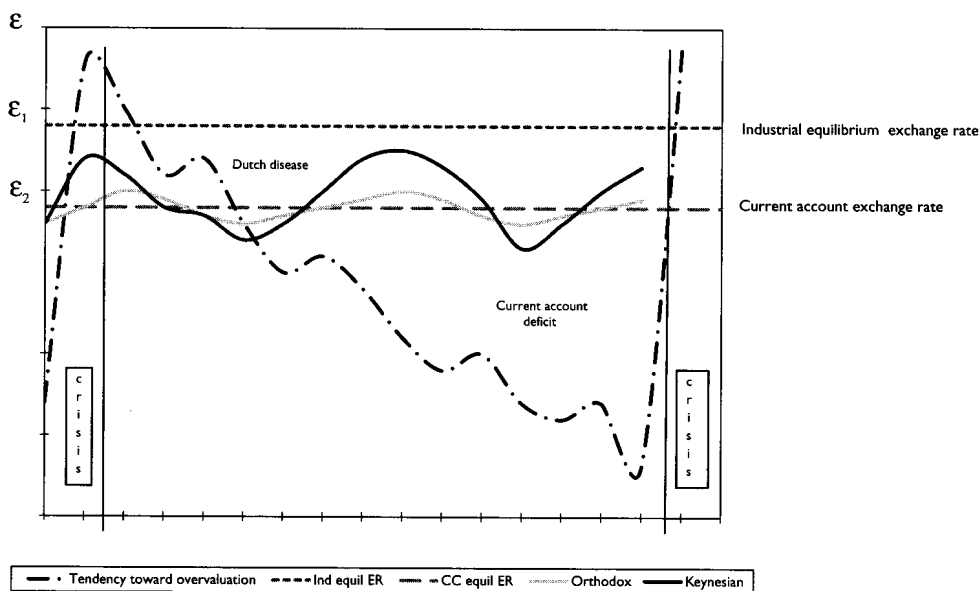
## **Summary Graph**

To summarize, the really balanced exchange rate in developing countries is the industrial equilibrium, not the current equilibrium exchange rate. If the exchange rate is left fully free, what controls it is not the market but balance-of-payments crises. The exchange rate is not just volatile; it lurches from sudden stop to sudden stop. In the crisis, there is a sharp devaluation. Then, in the next years, we see the tendency to the overappreciation to work: first, the Dutch disease appreciates (pulls down in the figure) the exchange rate up to

the current equilibrium. Second, excessive capital inflows produced by the policy of growth with foreign savings, high domestic interest rates, the use of the exchange rate as a nominal anchor, and exchange rate populism are the main causes of the additional appreciation of the exchange rate and its fall into the realm of increasing current account deficits. In consequence of all this, the exchange rate tends to be chronically overvalued. Figure 1 makes this easier to understand. It shows the two equilibrium rates: the industrial equilibrium and the current equilibrium. We have the effective exchange rate, which goes through the cycle of overvaluation and crisis. And, in dotted lines, we have the two theoretical alternatives to this tendency that is at the core of structuralist development macroeconomics: the soft and well-behaved fluctuation presumed by orthodox theory, and the volatile fluctuation presumed by the Keynesians.

As we see in Figure 1, the cycle begins with a balance-of-payments crisis or a sudden stop to the rollover of the country's foreign debt and the ensuing violent devaluation that usually takes the exchange rate above the industrial equilibrium. Next, the Dutch disease and capital inflows pull down the exchange rate, appreciating it.<sup>4</sup> Although it is not possible in practice to separate the effects of the two factors, for simplicity's sake we may assume that the Dutch disease pulls the exchange rate to the current equilibrium (since it is consistent with the long-term equilibrium of the exchange rate), while capital inflows pull it down into the area of the current account deficit and of increasing foreign indebtedness.

Theoretically, a floating exchange rate would prevent this appreciation and avoid the crisis, but only on the condition that markets endogenously balance financial markets. We know that this is not the case. A more realistic theory tells us that lending to developing countries is often a speculative practice involving the formation of financial bubbles. Foreign lenders see their prophecy that the exchange rate will continue to appreciate confirmed and keep lending, gaining from high interest rates and the appreciation of the local currency. They will continue to lend until, all of a sudden, in a well-known herd movement, they lose confidence and suspend the rollover of their loans, and the currency crisis breaks.



**Figure 1. Cyclical Tendency to Exchange-Rate Overvaluation**

## New Developmentalism

In the framework of globalization, countries compete among themselves. Hence, a national development strategy becomes even more necessary than it was before. New developmentalism is the name of this strategy, whose theoretical foundations lie in structuralist development macroeconomics. The essential feature of this strategy is that it neutralizes the two structural tendencies—the tendency of wages to grow more slowly than productivity and the tendency to the cyclical overvaluation of the exchange rate. Table 1 summarizes the policies of the new developmentalism and compares them with the conventional or Washington Consensus policies and reforms.

First row: In the conventional orthodoxy, the state is supposed just to ensure the good operation of market; in new developmentalism, the state is supposed to invest less in state-owned enterprises than it did in the Industrial Revolution, while retaining a strategic role in promoting economic growth. It has a major role in neutralizing the tendency to the cyclical overvaluation of the exchange rate, and it continues to have a strategic role in creating investment opportuni-

Table I

**New Developmentalism and the Washington Consensus**

<b>Conventional orthodoxy</b>	<b>New Developmentalism</b>
1. The state is supposed just to guarantee property rights and contracts	Strategic role for the state in economic development
2. Fiscal responsibility: primary surplus	Fiscal responsibility: primary surplus and positive public savings to finance public investments
3. Exchange rate irresponsibility: current account deficits financed by foreign savings	Exchange rate responsibility: current account balance or surplus insofar as the Dutch disease is neutralized
4. Monetary policy: one objective, to control inflation; one instrument, the interest rate	Monetary policy: to control inflation, to prevent financial crises, and to ensure a competitive exchange rate
5. No wages or incomes policy	Wage policy and incomes policy: to neutralize the tendency of wages to grow more slowly than productivity

ties and in ensuring the neutralization of the tendency of wages to grow more slowly than productivity.

Second row: Both the conventional orthodoxy and new developmentalism defend fiscal responsibility, but whereas the conventional orthodoxy limits itself to ensuring a primary surplus that keeps the debt/GDP ratio constant, new developmentalism seeks, in addition, positive public savings that allow the state to finance investments in capital-intensive, noncompetitive industries.

Third row: As for the exchange rate, the conventional orthodoxy is populist and contradictory: populist because it sponsors irresponsible current account deficits; contradictory because if it opposes high public deficits, if it is correctly opposed to the state spending more than it collects in revenue, it should also oppose current account deficits—the nation-state spending more than its income. Although conventional economic policy making rhetorically defends economic austerity, in practical terms it favors the two deficits, because once a country has a current account deficit, it will tend to have a budget deficit. In contrast, new developmentalism defends a responsible exchange rate policy: if the country is threatened by the Dutch disease,



it should have a current account surplus; if not, the current account deficit should be near to zero. I explain this below.

Fourth row: As to monetary policy, according to the conventional orthodoxy, its sole purpose is to control inflation, using a sole instrument, the interest rate. In new developmentalism, monetary policy should have three objectives: controlling inflation, preventing asset bubbles and financial crises, and keeping the exchange rate competitive, around the industrial equilibrium level, so as to ensure full employment and growth. To attain these objectives, it should pragmatically use all available instruments, the interest rate, control of credit, and so forth.

Fifth row: Finally, in relation to wages policy, the conventional orthodoxy is concerned just with “adding flexibility” to the labor market, that is, with reducing wages. In contrast, given the tendency of wages to grow more slowly than productivity, new developmentalism asserts that income policies are necessary to neutralize the labor market, such as a minimum wage, a basic income, and an increase in social expenditures in education, health care, unemployment compensation, and the training of workers dismissed for technological reasons. The latter two policies are preferable to policies that increase the wages bills of business enterprises.

A basic question remains: given the adoption of the growth with domestic savings strategy and the neutralization of the Dutch disease, how will the country be able to increase its rate of investment? The answer lies in the exchange rate itself. A country that keeps its exchange rate around the industrial equilibrium will have higher savings and investment rates than those of a country that keeps its exchange rate chronically overvalued. Thanks to a competitive exchange rate, investment opportunities will immediately increase for efficient enterprises, because the entire external demand will be within the reach of those enterprises. Now, when the investment rate increases, duly financed, total income will increase, and the savings rate will follow. Therefore, the right way to increase the country's savings rate is not by resorting to illusory foreign savings, but by ensuring domestic demand and business enterprises' access to markets. Enterprises will invest insofar

as the domestic financial system makes credit available. In the case of highly innovative business enterprises, innovation will “create” this demand internally, but these are exceptional cases. In the case of regular business activities, investment and growth will depend on a sustained internal market and an exchange rate that ensures competent business enterprises’ access to foreign markets.

In the growth process we should clearly distinguish the policies that accelerate economic growth from those that maintain it at a level deemed satisfactory. China, for instance, has no reason to increase its investment and growth rates, while in Brazil there is a consensus that the country should increase the investment rate from 18 percent to 25 percent of GDP: The state should increase its investments from the current 2 percent of GDP to nearly 5 percent (nearly a fifth of the total), while the private sector would be responsible for the rest (20 percent of GDP). New developmentalism is concerned with the acceleration of economic growth, but its models also apply to middle-income countries that are growing satisfactorily.

## **Is It Possible to Change the Macroeconomic Policy?**

Making new developmentalism the country’s basic economic policy depends on persuading its civil society of its superiority to the conventional orthodoxy. Yet it is no easy task to convince business entrepreneurs, the intellectual and professional middle classes, and the unions that this is the case. The hegemony of the conventional orthodoxy is well established, despite its repeated failures. But heterodox policies also frequently fail, and new developmentalism must not be confused with, for instance, a kind of vulgar Keynesianism that sees in budget deficits the solution to all problems (just as the conventional orthodoxy sees in reducing budget deficits the solution to all problems). New ideas take time to be accepted. In the 1990s the ideological hegemony of neoliberal ideas and neoclassical economics was practically absolute. The situation has changed since the early 2000s, when the failure of the Washington Consensus to promote economic development and ensure financial stability became evident.

It definitely changed when the global financial crisis showed that even for the rich countries, market deregulation had been a huge mistake. The market is a wonderful institution to coordinate complex economies, provided that it is duly and carefully regulated.

Today the conventional orthodoxy is no longer hegemonic, but structuralist development macroeconomics and new developmentalism are not yet able to replace it. This is mostly because structuralist development macroeconomics consists of a set of models, and new developmentalism consists of policy prescriptions, which have only recently become consolidated from a theoretical point of view.

In new developmentalism's transition toward hegemony, its proponents also face an issue often raised by its interlocutors in civil society. They agree that its theories and prescriptions make sense, but they doubt that they can be put into practice, that the exchange rate can be managed. This "impossibility" is, therefore, the last bastion of the conventional orthodoxy, but it is a fragile one. New developmentalism advocates applying controls to capital inflows, not to capital outflows, because, when the exchange rate is competitive, balance-of-payments crises cease to be the natural condition of the middle-income countries. Historical experience shows that the control of capital inflows is difficult but viable. However, although there are domestic political difficulties in imposing export taxes on commodities that give rise to the Dutch disease, many countries already do it—although the tax rate often has just a fiscal objective and is insufficient to neutralize the disease. The opposition of the local producers of the commodity tends to be strong, but we have already seen that they will not lose from the tax. In fact, the producers of primary goods will benefit as long as the government uses some of the tax's revenues to set up a stabilization fund that would help them in the event of a violent drop in the commodity's international prices. Finally, the shift of the current equilibrium exchange rate toward the industrial equilibrium generates two temporary difficulties: A cost shock will cause a one-time increase in inflation, and it will slightly decrease real wages. But inflation would soon fall again, provided that all instances of price indexation were abolished. And wages would soon rise again, now in

a sustained way, thanks to the increased investment rate and the accelerating growth rate.

## Notes

1. The Ten Theses are available at [www.tentheseesonnewdevelopmentalism.org](http://www.tentheseesonnewdevelopmentalism.org).

2. Among others, Paul Rosenstein-Rodan, Ragnar Nurkse, Arthur Lewis, Gunnar Myrdal, Michal Kalecki, Arthur Prebisch, Celso Furtado, Hans Singer, and Albert Hirschman.

3. See Luiz Carlos Bresser-Pereira, *Globalization and Competition* (Cambridge: Cambridge University Press, 2010), and idem, "Structuralist Development Macroeconomics," 2012, available at [www.bresserpereira.org.br](http://www.bresserpereira.org.br).

4. Note that I am measuring the exchange rate dividing the national money for the dollar or for a basket of currencies, not the inverse as is usually done in developed countries.

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