Economic Convergence

Economist

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Consequences of growth

- Nowhere are the consequences of different rates of growth clearer than on a trip up the Pearl River Delta in southern China.

Hong Kong and Guangzhou

- At the river's mouth sits Hong Kong: average living standards exceed those in most rich European countries
- Shenzhen (a special economic zone since 1980): incomes are just over half of those in Hong Kong.
- Farther north and west sits Guangzhou: a quarter of HK.
- Toward the western edge Yunnan: a tenth of those in Hong Kong

The glorious fifteen

- The glorious fifteen
- Over the past 15 years, when adjusted for living costs, output per person in the emerging world almost doubled between 2000 and 2009; the average annual rate of growth over that decade was 7.6%, 4.5% higher than the rate seen in rich countries
- The gap between the developed and developing worlds narrowed quickly

Against deprivation

- The share of the developing world's population living on less than $1.25 a day (the international definition of poverty) has fallen from 30% in 2000 to below 10%
- Were the emerging world able to maintain a 4.5% growth advantage over the rich world, its average income per person would converge with that in America in just over 30 years

Hopes slipping away

- However, when the new ICP estimates are applied, the average GDP (PPP) per head in the emerging world grew just 2.6% faster than American GDP in 2013
- The most recent 2014 growth projections from the IMF suggest the outlook is darkening further
- Excluding China, it will take more than 300 years for full convergence

Modern economic history

- Feature of modern economic history
- Lant Pritchett (1997): describing a widening income gap between rich and poor countries as "the dominant feature of modern economic history" (1800–2000)
- Orthodox economics struggled to explain it
- Theories of economic growth like Robert Solow (1956) predicted that, over time, poor economies should catch up with rich ones

Solow model

- Solow model: economies were poor because their workers had access to less capital
- This capital shortfall implied that the return on investment should be high, so capital should flow from rich countries to poor ones, leading the two worlds to converge

Convergence in rich countries

- The model seemed to apply well enough to the histories of then-rich countries
- Convergence: Britain, US, and other European countries in the late 19th and 20th century
- But what was true for Europe did not apply elsewhere
- Some Asian economies proved to be exceptions: South Korea, Taiwan, Singapore and Hong Kong

New Models

- Solow model can not explain the dominant feature of modern economic history
- New models (to explain the dominant feature):
  - human capital
  - institutions
  - geography and climate