India and the Global Economy

Interview with Augusto Lopez-Claros, Chief Economist, World Economic Forum

Economic Times of India, January 2004

Q: The WEF's global competitiveness report was first published in 2000 if I am not wrong. What happened in 2000 that made you come up with an index on World Competitiveness?

A: The World Economic Forum has been putting together competitiveness indices since 1979. Over time the number of countries covered has expanded, the range of questions included in the Executive Opinion Survey has broadened and deepened, and the methodology used to construct the indices has evolved and become more sophisticated. Perhaps what is significant about the year 2000/01 is that that is the period when the Forum cooperated closely with professor Jeffrey Sachs of Harvard University. He provided advice to the Forum on the construction of the "growth competitiveness index" which we currently use to capture a country's medium to long-term growth potential. By capturing elements of the macroeconomic environment, the quality of a country's public institutions, and the level of technological readiness the index does a reasonably good job of identifying the key elements that go into making a country competitive.

Q: Moving on to methodology, in 2003, you have modified the factors affecting competitiveness. You have decided to capture public waste rather than public expenditure as a percentage of GDP to measure competitiveness. Any particular rationale for that!

A: We would prefer not to have to tamper with the index ever, or hardly ever, so as to be able to make intertemporal comparisons that reflect purely changes in each country's circumstances, rather than a combination of these and methodological innovations. However, in some cases, there may be compelling reasons to make changes in the way the index treats a particular variable. This was the case last year (2003) with government expenditure, where we moved away from a sole focus on the level of government expenditures, to the development of a subindex which captured in some fashion the efficiency (or wastefulness, if you wish) of spending. In our earlier formulation we were rewarding countries with low levels of spending linked to nonpayment of wages, pension arrears, and so on, and penalizing the likes of Sweden and Denmark, where government spending may be high but is not transparently inefficient. Because of this, in reporting our results, we were careful to present the data in a way that allowed the reader to control for changes in methodology, so as to isolate "true" changes in rankings.

Q: As an extension to the above question – does including public waste – reflect on WEF's increasing concern over the effects of rapid growth on the environment? For example the rise of the new Asia and its impact on the region's environment!

A: Successful economic development involves a great deal more than just trying to manage effectively the macroeconomic environment. Over the last couple of decades we have learned that there are other building blocks that are essential to generate a process of sustainable development. It matter a great deal, for instance, whether people can determine who should govern them and on what principles. Without the sense of legitimacy that comes from this governments will not be able to govern effectively. It does matter whether governments open to public scrutiny the accounts and activities of public institutions. Transparency is the term that we use to describe this and Amartyn Sen has spoken, in this context, about the need for society's members to deal with one another under "guarantees of disclosure and honesty", to prevent corruption and abuse. Care for the environment is one additional component of what I call the "development agenda". We fool ourselves if we maintain a narrow focus on economic growth per se and neglect the fact that, often, an unintended by-product is a sharp deterioration of our environment. My concern here is that, because Asia is the region projected to have the highest growth rates over the longer-term, the potential adverse impact on the environment will be the greatest. We have already seen the transformation of Bangkok's pristine canals into open sewers and read in the press about the smog cloud that hangs over much of Asia throughout the year and which can be detected from satellite photography. And let's not speak about the traffic jams in some of the Asian capitals which are gradually taking us to the early part of the 20th century in terms of the speed of travel. Unless we factor in the costs of these effects (on public health, on the quality of life, on the ability of governments to provide basic services to their respective populations) and make provisions to deal with their effects in the future, we will be simply postponing the day of reckoning, effectively passing on to future generations the solution of problems which we should be addressing now.

Q: Right, it seems that Asia is a cause of concern for you, as much for its spectacular rise and more so for the pitfalls that are coming along with it. In a global competitiveness study, as like yours, how do you decide on which region to focus on – during every round of the study? What's the modus operandi inside WEF – perhaps you can throw in some lights about the decision making route.

A: Our main study, the Global Competitiveness Report, does not focus on a particular region per se. As its name highlights, it is a global perspective on competitiveness based on our annual Executive Opinion Survey. In its latest incarnation, it covers 102 countries and, thus, is the most comprehensive study of its type. The report has two parts; a statistical compendium that reports on the results of competitiveness rankings, the hard data that goes into computation of the index and also includes individual country profiles, outlining the results of the Survey for each of the 102 countries. The second part is a collection of articles from top experts in their fields writing on the key issues of the day and shedding light on some of the main topics arising in the economic and development agenda. I see this part as an essential complement to the rankings and the data, providing important intellectual content to our reports. In addition to the Global Report we also do regional competitiveness reports, although these are not annual in nature. We have done one on Latin America, Asia, the Arab world and are presently preparing one on Africa, in preparation for our Africa Economic Summit in Mozanbique later this year. We have also recently issued a Global Information Technology Report, containing the first index ever measuring nations' "network readiness".

Q: Are their any sections in the methodology which bother you! Something which you would like to incorporate in your Competitiveness Index at some point of time.

A: Yes. At the moment the index does not capture well enough "sustainability" aspects of development. I would like to have an index that gives credit to countries like Chile that are doing an extremely good job of managing their forests, lakes and other aspects of their habitat and penalize countries that are burning their forests and violating the environment in some other way. This is part of our next project.

Q: And nothing about the rising income disparity!

A: This is clearly a key issue. Whereas in 1960 the income of the top 20% of the world's population was about 30 times higher than that of the bottom 20%, by 1995 this ratio had risen to 82 before scaling new heights early in the new century. who will pay for all of these initiatives? So, what how do we confront this issue?. First, the developing countries themselves, hosts to billions of people who feel left behind by the locomotive of globalization, can do a great deal more to improve economic management and to better use available resources. According to figures compiled by the UNDP the developing world spends more on defence and the maintenance of military establishments every year (over US$200 billion) than it does on health and education combined. There are just too many examples in the developing world that resemble the recent case of a relatively small country in Latin America which, during the 1990s, spent US$500 million modernizing its air force. Not only is the figure painfully large in relation to the size of its economy, but the expense will entail a much larger claim on the budget over the next decade, because of the need to service the associated military debts, as well as on-going expenses for maintenance, spare parts and training, all for a project with virtually zero social benefits. It boggles the mind to think how many hospitals could have been supplied and schools built and children provided with access to the internet for the sum of US$500 million. One cannot but agree with George Soros when he states that: "By far the most important causes of misery and poverty in the world today are armed conflict, oppressive and corrupt regimes, and weak states—and globalization cannot be blamed for bad governments."

That developing country governments bear a heavy burden of responsibility for the plight of the poor and the meagre fruits of development, does not exempt the donor governments—mainly in the industrial world— from their own share of culpability. First, rich countries' commitment to assisting the developing world is much weaker today than at any time in the post-War period. To cite a well-known example: the United States provided close to 3% of GNP in development assistance in 1946; by 2001 this figure had come down to around 0.1% of GNP or nearly 30 times less. Whereas the rich industrial countries currently spend US$200 billion plus a year on subsidizing their agriculture they spend about US$52 billion on foreign aid. (That subsidies to relatively well-off farmers in the industrial world distort the markets for agricultural commodities and impose a heavy financial burden on farmers in the developing world is something that only recently has begun to receive a measure of attention.) Second, what little aid is provided is often misspent, with little to show for it in terms of improved policies, living conditions, and so on. So, the scope would appear to be enormous for improvements in both the volume and the efficiency of rich country aid flows.

Q: Well, allow me to say this, but such concerns and demands have been there for a long time now. Two questions, does domestic demand in developed economies indeed have the capacity to sustain foreign supply. And if yes, do you think that rather than a World Trading Organisation – the future is in regional trading blocs – somewhat closer to flourishing Free Trade Organisations maybe!

A: Yes, you are right in saying that these concerns are nothing new. But I must stress that regional trading blocs or FTAs can co-exist with a World Trade Organization and the multilateral approach to trade liberalization that has underpinned the remarkable expansion of global trade in the last 50 years. Do you know that even the United States, Canada and Mexico—the 3 founding members of NAFTA—one of the largest free trade areas in the world are the countries that use the dispute settlement mechanisms of the WTO with the greatest regularity. So even they have discovered that a multilateral setting for trade negotiations is a very useful devise. What is needed is to supplement existing arrangements within the WTO with a more ambitious opening of markets for certain goods in the developed world, particularly agriculture, to do away with what Joseph Stiglitz calls "the global inequalities and the hypocrisy of the advanced industrial countries."

Q: Fine -- so you say that a multilateral setting can co-exist with a regional trading bloc. Can we then see a cooperative index coming from the WEF in future which measures cooperative competition among regional across the world and indexing the regions – rather than the current competitiveness index which pits nations against each other on an index?

A: Umm…. (long pause) that's an interesting thought. Our current unit of analysis for comparison purposes is the nation-state but this may well change. I can imagine that if the European Union continues along the path of cooperation and integration that it has pursued since it was created in 1957, at some point it might emerge as a United States of Europe, where Sweden and France will be, within the Union, the political equivalent of Michigan and California within the Unites States of America. We in Latin America consider the European model of economic and political integration a useful model for the region. After all, 11 out of the top 19 economies in the world with the highest per capita income come from European Union—this means that the European experiment of bringing barriers down, creating a large and fully integrated economic and legal space has been fantastically successful in promoting prosperity. Why not emulate its best parts and adapt it to Latin America, Africa, Asia and so on? There would appear to be no compelling reason.

Q: Do you really think such indices from WEF/sovereign ratings from Standard and Poors or Moodys /country risk measures as the BERI model from the Economist Intelligence Unit – really serve any purpose?

A: Yes they do. Speaking for our own work, the publication of the results every year generates not only immense public attention but internal debates about the need for reforms in countries as varied as France, Germany, Canada, China and Argentina. Our Survey provides interesting insights about each country's strengths and weaknesses and thus helps identify for policy makers the most urgent priorities for reform.

Q: Finally, finally can we see a day when WEF summit occurs in Bombay! – Especially with the World Social Forum happening these days in the city! What's your take on India's economic rise in the end!

A: (Smiles…) No, I think that for the foreseeable future the annual meeting of the WEF is likely to stay in Davos, Switzerland. However, please note that we have an annual gathering in Delhi—the India Economic Summit. As regards India, I think after years of cautious macroeconomic management and structural reforms the benefits are beginning to show, particularly as regards growth, which is tremendously important in India because it is what in the end is going to make the greatest difference in terms of reducing the incidence of poverty, which should be and remain the chief priority of the government. I would just like to sound a word of caution though about the management of the public finances. India has been running deficits for the general government to the tune of 10% of GDP for the last several years running. A growing economy has helped sustain these but I think the IMF is right when they say that "India's large fiscal deficits and public debt are exacting an economic cost in terms of foregone growth." I hope that the WSF's annual global summit, which is happening in India is giving some attention to these issues.