Is There a 'Davos' Economics?

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What are the factors, policies and institutions which best contribute to boost productivity and thus economic growth? How can governments best ensure that their countries will be sufficiently competitive to be present in an increasingly sophisticated global economy and generate enough resources to support poverty reduction and rising levels of income per capita? As chief economist for the World Economic Forum and editor of the annual *Global Competitiveness Report* I have travelled widely during the past three years, meeting with senior government officials and business leaders to discuss their countries' strengths and weaknesses as they seek to create an environment supportive of private sector economic activity. What are the secrets of success? Why is it that some countries seem able to do so much better than others in sustaining rising levels of well being for their respective populations?

Here are 8 important lessons:

Lesson 1: Do not live beyond your means. The vast majority of the emerging market crises of the past decade have had as their primary cause the inability of governments to manage the public finances in a responsible way. Either because the state is not able to collect adequate levels of tax revenue, or public spending is out of control or some combination of the two, the fact is that large budget deficits are lethal for growth. Over time, they lead to rising levels of public debt which, in turn, constrain the ability of the government to allocate sufficient resources to education, public health, and infrastructure—three areas that are key to efforts aimed at enhancing the economy's competitiveness. In an era of integrated financial markets and savvy investors looking for high yields everywhere, markets will punish fiscal indiscipline harshly, as Argentina and Turkey learned in 2001.

Lesson 2: Low taxes are not a miracle cure. There is little evidence that low taxes, in and of themselves, will contribute to growth. Some of the most competitive economies in the world—the Nordic countries, for instance—have high revenue ratios but their governments have been extremely efficient in the way they have gone about using the resources thus generated. It obviously will matter a great deal for growth whether a given level of tax revenue is used for education and training and to provide a first class telecommunications infrastructure, or is frittered away in unproductive ventures or, worse, simply stolen. The extensive social safety net provided by the Nordic countries to their populations is not an essential prerequisite for growth; it is more a political choice made in the context of highly developed democracies. What is key is the efficiency of resource use. Nigeria has generated hundreds of billions of dollars of oil revenues over the past several decades but it has had a dismal growth performance.

Lesson 3: Corruption is a killer of growth. When I joined the IMF in the mid-1980s as a young economist, corruption was a taboo subject. Countries may have been be ruled by thieves but one was told to suspend political judgements and to focus on the technicalities of tax or monetary policy. Today there is broad consensus that open and transparent government is central to successful development, that only honest governments have the credibility to ask for sacrifices because their leaders will be perceived as working for the public good and thus worthy of support. Where corruption thrives, paying taxes is seen as bad business and individuals and companies will expend considerable talent and effort in finding creative ways to fool the state. This, in turn, will undermine the state's ability to respond to pressing social needs. Chile has had the best growth performance in Latin America in the past 15 years; it is also, according to Transparency International, the least corrupt emerging market in the world.

Lesson 4: The virtues of judicial independence. For the business community it matters enormously whether access to the judicial system can lead to speedy resolution at reasonable cost and in a way that ensures outcomes consistent with the law. Cases that sit in the courts for a decade, that consume inordinate time and money and that may, in the end, reflect the relative power and influence of the parties concerned add to business costs and undermine competitiveness. In Germany, the business community may be unhappy with inflexible labour markets, but they benefit from a first class judicial system. In Russia, on the other hand, justice is for sale, as it is in many other developing countries.

Lesson 5: The evils of red tape. The World Bank's *Doing Business Report 2006* highlights the high costs of red tape and mindless bureaucracy. The World Economic Forum's own annual Executive Opinion Survey provides corroboration for the notion that it is precisely in those countries where the emergence of new businesses and an entrepreneurial class is most desperately needed that governments will often erect the most onerous obstacles to the creation of new firms. This problem is particularly acute in Latin America, a region with a steeped culture of red tape. For governments the challenge is to strike the right balance between the need for some regulation—for instance, aimed at consumer protection or safeguarding of the environment—and to avoid excessive bureaucracy which stifles investment and kills the entrepreneurial spirit.

Lesson 6: Education as the central pillar. Investment in education is turning out to be the key driver of productivity. As the global economy becomes more complex it is increasingly necessary to upgrade the level of training of the labour force, to ensure that its members can adopt easily the latest technologies and avail themselves of the opportunities existing in a rapidly integrating world. The returns to investment in education and training are extremely high and governments that have given appropriate attention to this are now reaping rich rewards. Korea, a country without natural resources and a difficult political geography has become a global industrial power. Taiwan has practically cornered the market for the production of the dozen or so most important pieces of ICT hardware for the modern office environment, and Israel has close to 150 high tech companies listed in the NASDAQ, more than any other country save the US and Canada. In all cases, high levels of collaboration between the business community and the universities and strong government support for higher education have played an absolutely essential role.

Lesson 7: Computers and mobile telephones as the new engines of growth. Illiteracy has fallen dramatically in the post-war period and coverage of primary education has risen everywhere. Now the focus needs to broaden to empowering people through the adoption of new technologies, from access to the internet to mobile telephones. There is a high correlation between the ranks achieved by countries in the World Economic Forum's Global Competitiveness Index and the penetration rates of these technologies, which contribute to enhance productivity growth. The scope for increased public spending in this area is huge, given still inordinately high levels of expenditure on defence and other unproductive items.

Lesson 8: Empowering women. There is well established empirical evidence that the most profitable investment a country can make is to educate its women, particularly its girls. Female education, employment and ownership rights greatly empower women and allow her to shape her environment. Literacy helps reduce fertility rates, including the bias against female child mortality. Competitiveness is about efficient resource use, including human resources. Where women are empowered to participate in the economy and the political process, productivity and growth will benefit.

Globalization has enhanced our ability to learn from each other. The successful development experiences of the past 40 years are well documented and, by now, well known. What is often lacking is political will and good governance. But the options are there and those governments making the correct choices are unleashing processes of self-sustaining growth, for the benefit of their respective peoples. In the age of globalization those countries that frame policies mindful of the above lessons will continue to prosper; for others the development process will be slower and their societies will fall behind.

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