

# Models of the developmental state

Luiz Carlos Bresser-Pereira

## Abstract

This paper seeks to understand the developmental state and its historical role in industrial revolutions and afterwards. First, the developmental state is defined as an alternative to the liberal state. Second, it is argued that industrial revolutions have always taken place within the framework of a developmental state. Third, four models of developmental states are defined according to the point in time at which the industrial revolution took place and the central or peripheral character of the country. Fourth, the paper describes how the state withdraws partially from the economy after the industrial revolution, but the developmental state continues to have a major role in directing industrial policy and in conducting an active macroeconomic policy.

---

## Keywords

Public administration, economic planning, macroeconomics, liberalism, nationalism, economic policy, economic development

## JEL classification

O10, O11, O19

## Author

Luiz Carlos Bresser-Pereira is an Emeritus Professor with the Department of Economics of the Sao Paulo School of Economics, Getulio Vargas Foundation, Brazil. Email: Bresser-Pereira@gmail.com.

## I. Introduction

In the 1950s, Brazilian political scientists and economists identified “developmentalism” as a set of political ideas and economic strategies that drove Brazil’s rapid industrialization and underpinned the coalition of social classes identified with national development. Hélio Jaguaribe (1962, p. 208) stated in the early 1960s that “the core thesis of developmentalism is that the promotion of economic development and the consolidation of nationality stand as two correlated aspects of a single emancipatory process”. Through “national developmentalism”, which would become the established term for the country’s development strategy, Brazilian society was successfully overcoming the patrimonial state that characterized its politics until 1930. Other Latin American countries such as Mexico and Argentina and East Asian countries such as South Korea, Taiwan and Singapore grew by embracing a developmental strategy that was theoretically grounded in a combination of structuralist development theory and Keynesian macroeconomics. These countries combined state intervention with a dynamic private sector, modelling themselves on Japan. In the early 1980s, Chalmers Johnson (1982), in an attempt to understand its extraordinary economic development, called the Japanese state a “developmental state”.<sup>1</sup> Yet, notwithstanding the extraordinary success of these countries, over the 30 neoliberal years of capitalism (1979–2008), developmentalism became a derogatory term synonymous with fiscal irresponsibility or populism. This rhetorical manoeuvre was a way of reaffirming the new neoliberal and neoclassical hegemony, but was not entirely groundless. Indeed, from the late 1970s, faced with the crisis brought about by the second energy shock, several Latin American countries refused to carry out the required macroeconomic adjustments and embraced populism in the name of Keynesianism, giving rise to a major foreign debt crisis in the 1980s that created the conditions for neoliberal hegemony in the region. In the 1990s, the liberal state and its neoliberal policies and reforms failed to make good on their promises, instead indulging in current account deficits and exchange-rate populism,<sup>2</sup> and the outcome was sluggish growth, great financial instability and a marked increase in inequality. In the early 2000s, developmentalism resurfaced both as an existing historical phenomenon and as a theoretical framework and development strategy. In the former manifestation, it was associated with leftist governments that might be identified with “social developmentalism”, often sliding into fiscal populism; as regards the latter, economists and other social scientists, including the author of this paper, proposed a new theoretical approach to the problem that came to be called “new developmentalism” — an alternative to Latin America’s “classical developmentalism” or “structuralism”.<sup>3</sup>

New developmentalism is an attempt to refresh development economics. Its developmental macroeconomics is based on the tendency towards cyclical and chronic overvaluation of the exchange rate. It focuses on the five macroeconomic prices — the profit rate, the interest rate, the exchange rate, the wage rate and the inflation rate— that the market is unable to get right. Its political economy is based on the concepts of the developmental state and developmental capitalism.

Taking the countries that industrialized first (England and France) as benchmarks, the historical path they have followed may be summarized in a few stylized facts. In the late Middle Ages, absolute monarchies allied with the nascent bourgeoisie to overcome feudal lords and form the absolute and mercantilist state. The industrial revolution took place within the framework of this first developmentalism: mercantilism. A liberal state became dominant in the 1830s and lasted for 100 years. The New Deal

<sup>1</sup> The term State is usually written with an upper-case “s”, which seems reasonable as a designation of a society’s greatest institution. In speaking of the developmental state or the patrimonial state, and indeed the nation-state, however, what is meant is a political system or form of government in the former case and a form of sovereign political-territorial society in the latter, so the lower case will be used in these instances.

<sup>2</sup> The concept of exchange-rate populism originates from the works of Adolfo Canitrot (1975) and Carlos Díaz-Alejandro (1981). The concept is central to the new developmentalism, whose macroeconomics focuses on the foreign exchange rate and on current account deficits or surpluses.

<sup>3</sup> See Bresser-Pereira (2016).

emerged from the Great Depression and the golden age of capitalism from the Second World War. This was the second developmentalism, marked by moderate state intervention in the economy, an active macroeconomic policy, financial stability, fast growth, moderate reduction of inequality and a developmental and social class coalition: Fordism.<sup>4</sup> This new phase was to last for about 30 years before once again giving way to economic liberalism, which lasted for a like period before entering a deep crisis with the global financial crisis of 2008.<sup>5</sup>

This paper will not cover each phase of the long-term process. Its purpose, rather, is to convey the logic of the developmental state within the framework of capitalism, the four historical forms that it adopted when it led the industrial and capitalist revolution, and the fifth developmental model that came after the Second World War. Its two institutions of economic and social coordination are the state and the market. While the market is devoid of will (albeit not of the interests of those operating in it), the state represents the law and, therefore, political will. It is through the state that collective action takes place and that nations regulate social life in pursuit of the political objectives that modern societies have set for themselves: security, liberty, well-being, social justice and protection of the environment. It is through the market that companies compete, prices are formed and resources are efficiently allocated across the various competitive sectors of the economy. It is through the market that the economy's competitive sectors are coordinated, and it is through the state that the market is regulated, non-competitive industries are coordinated and active macroeconomic policy can operate to ensure macroeconomic balance and create the conditions for private sector investment and innovation, full employment and sustained economic development.

## II. What is the developmental state?

The presence of the developmental state throughout the history of capitalist development is not the product of chance. The logic of the nation-state is that of economic development and competition. As Ernest Gellner (1996) put it, the nation-state is opposed to the classical, or pre-industrial, empire. The empire is the political-territorial unit that characterizes more developed ancient societies (those that Gellner refers to as “agro-literate societies”), whereas the nation-state is the political-territorial society of capitalism. The logic of nation-states is one of economic growth that the state, as an organization and as manifested in laws and policies, must foster. In regulating capitalist economies, the modern state assumes two basic forms, the developmental and the liberal, that are also the two forms of economic and political organization for capitalism, given that the state is the fundamental institution of modern societies. The liberal state limits itself to guaranteeing property rights and contracts, controlling the national currency and maintaining healthy public finances, leaving all other activities to the coordination of the market. Chalmers Johnson (1982 and 1999) defined the developmental state as a state that has economic development as a priority objective; intervenes in the economy not only by means of regulation, but also directly; has a small and highly skilled public bureaucracy to which actual powers are assigned, leaving the legislature and judiciary in the background; controls its foreign commercial and financial accounts and, therefore, the exchange rate; protects domestic manufacturing industry from end products; facilitates machinery imports; separates foreign technology, in which it has a strong interest, from foreign capital, in which it has no interest; creates state-owned financial institutions; adopts credit and fiscal incentives, but always on a temporary basis, subject to constant assessments; adopts a consolidated public investment budget; offers strong government support for science and

<sup>4</sup> Fordism was the name given by the French Regulation School to the “mode of regulation” of capitalism led by the United States from the New Deal to the 1970s. It was a developmental class coalition characterized by mass consumption, large monopolist and bureaucratic corporations and some reduction of inequality, insofar as wages grew with productivity and technical progress was capital-saving.

<sup>5</sup> See Bresser-Pereira and Ianni (2017) for a comprehensive review of historical forms of developmental class coalitions.

technology; and eschews detailed laws, leaving room for firms to take the initiative, with discretionary guidance from the public bureaucracy. Peter Evans (1992) has drawn attention to two characteristics of the twentieth-century developmental state, namely bureaucratic capacity and embeddedness: the way the public bureaucracy is enmeshed in society and the business community. Johnson and Evans credit the public bureaucracy with a strategic role in the developmental state, which is reasonable, but industrial entrepreneurs also have a decisive part to play.

These are excellent definitions of the developmental state, but it seems legitimate to define it in a broader way. The state will be developmental if it: (i) views economic growth as its main objective; (ii) intervenes moderately in the market by planning the economy's non-competitive sector and by adopting strategic industrial policies; (iii) operates an active macroeconomic policy by limiting budget and current account deficits and by getting "right" the five macroeconomic prices, particularly the exchange rate; and (iv) is politically supported by a developmental class coalition formed of entrepreneurs, workers, public bureaucrats and sectors from the old dominant class which holds political power and embraces a national development strategy, thereby standing in opposition to a conservative or liberal coalition made up of sectors of the pre-industrial dominant class, rentier capitalists and financiers.<sup>6</sup>

Following Evans (1992, p. 12), besides being developmental or liberal, the modern state may be "predatory" when it "lack[s] the ability to prevent individual incumbents from pursuing their own goals. Personal ties are the only source of cohesion, and individual maximization takes precedence over pursuit of collective goals". Predatory states exist in pre-industrial countries that have not yet had their industrial and capitalist revolution. Their rulers claim to be developmental or liberal, as convenience dictates, but this means little or nothing. History shows that the state has played a key role in all industrialization episodes; in other words, that all episodes of industrial take-off or revolution have taken place within the framework of a developmental state, beginning with the British Industrial Revolution, which took place in a context of mercantilism — the first historical form of developmentalism. There are good reasons for this. The market is an excellent institution for coordinating competitive economic activity, but is powerless when it comes to non-competitive activities, and is a poor coordinator of macroeconomic prices, while the change from an agrarian to an industrial society necessarily involves a national development project.

One important issue is whether agrarian elites take part in developmental class coalitions. As Marcus Janoni (2014, p. 99) noted, "in South Korea and Taiwan, the rural society converged with industrial progress, not seeking an independent political settlement". The same can be said of the German agrarian elites that Bismarck successfully brought into his political settlement. In Brazil, it is usually argued that the agrarian elites have opposed the developmental state, both in the pre-industrial period and currently. Where agriculture is concerned, however, a crucial distinction exists between countries like Brazil, on the one hand, and most European and East Asian ones, on the other. In these, agriculture is essentially domestic market-oriented, while in Brazil coffee and sugar cane in the past, and these two plus soybeans and orange juice at the present day, are export commodities and causes of Dutch disease — the long-term appreciation of the domestic currency that hinders industrial activity because these commodities can be exported at an exchange rate far stronger than the one at which competent industrial companies would be competitive. Dutch disease was neutralized in Brazil during a period of rapid development by means of a disguised tax on exports that the coffee growers called "foreign-exchange confiscation" — a tax that led them to oppose industrialization. From the 1930s to the 1950s, however, support from the non-exporting agrarian oligarchy was crucial to the success of Getúlio Vargas's national developmental pact.

The definition proposed here is not prescriptive, but rather a generalization of the behaviour of developmental states, particularly those in East Asia and Brazil at the time they industrialized. Assuming

<sup>6</sup> Conservative coalitions in developing countries are associated with the liberal international elites and are thus "liberal" insofar as they defend, even if they do not necessarily practise, economic liberalism.

that the behaviour of developmental states has not been too different, let us consider South Korea and summarize the measure that enabled it to successfully catch up: high import tariffs, in the range of 30% to 40% in the 1970s and 20% to 30% in the 1980s; plenty of non-tariff barriers; large export subsidies; small fiscal deficits; a low debt-to-GDP ratio; a strongly regulated financial market; low, often negative, interest rates; strict control of the exchange rate; strict control of capital inflows and outflows; and average inflation of 17.4% in the 1960s and 19.8% in the 1970s.<sup>7</sup>

### III. Models

When this broad view of the developmental and liberal states in their economic aspect is taken, a crucial fact emerges from the history of capitalist development: every industrial revolution — the decisive moment of the capitalist revolution in each country — has taken place under the leadership of a developmental state. England and France industrialized under mercantilism, which was the first developmentalism; Germany under Bismarckism; the United States under Hamiltonianism; Japan under the strong control of the Meiji state; Brazil and Mexico under national developmentalism.

To verify this, it is worth categorizing countries and developmental state models. Going by two criteria, namely the points in time when peoples gain autonomy, become a nation, form a nation-state and achieve the industrial revolution, and the position of the country in question at the centre or on the periphery of capitalism, it is possible to distinguish four developmental state models at the time of their industrial revolutions: (i) the original central developmental state model of the countries that industrialized in the eighteenth and early nineteenth centuries, such as England and France; (ii) the original latecomer central developmental state model of countries that were not colonies but achieved their industrial revolution belatedly, such as Germany and the United States; (iii) the peripheral independent developmental state model of countries that were colonies or quasi-colonies of developed countries, but achieved a high level of national autonomy, industrialized, caught up and became rich, such as Japan, Taiwan and South Korea, or became middle-income countries, like China, India, Malaysia and Thailand; and (iv) the peripheral national-dependent developmental state model of countries that did achieve the capitalist revolution but, after the deep foreign debt crisis of the 1980s, lost some of their national autonomy and started growing at a very slow pace, such as Brazil and Mexico. In addition to these four models of the developmental state according to the timing of the industrial revolution, there is a fifth model: (v) the welfare developmental state, after the Second World War. There are also pre-industrial countries that are trying to achieve the revolution right now and countries that are simply poor, but this article is not concerned with either of these.

#### 1. The original central model

With the first four developmental state models, the countries involved achieved a reasonable degree of autonomy and embraced a growth strategy in which the state and the market played important roles. The original central model has been the subject of study by many scholars, from great economists such as Adam Smith and Karl Marx to historians like Fernand Braudel, Paul Bairoch and David Landes. It unfolded within the framework of a mercantilist developmental state rather than a liberal state. The liberal critique of mercantilism — taken both as a historic phase of capitalism and as economic theory — is therefore misguided. The mercantilist, or absolute, state is that in which the emergence of market economies — the industrial revolution — takes place through intervention in the market to foster

<sup>7</sup> This summary is based on Ha-Joon Chang (2002b) and on a class at the sixth Latin American Advanced Programme on Rethinking Macro and Development Economics (Laporde), Sao Paulo, 11 January 2016.

national development. It rests on a coalition of classes formed by the monarch, his patrimonial nobility (whose revenues come from state coffers rather than land rent) and the large nascent bourgeoisie. Its overarching development strategy is to enlarge the domestic market by making the boundaries of the nation-state as wide as possible, the means to which include waging war upon neighbours in order to annex them. Notwithstanding the fact that it is creating a market economy, it does not hesitate to intervene in the economy and organize monopolies through which the partnership between the absolute monarch and the large bourgeoisie, which has paid taxes to fund the monarch's wars, increasingly takes shape. As for Adam Smith's radical criticism of mercantilist theory, it is quite understandable, not because he was "founding" economic theory (its founders were mercantilist economists), but because he was founding a new school of economics: the Classical school, whose members would include brilliant economists such as Malthus, Ricardo and Marx. It is, or should be, common knowledge, at least since Schumpeter's monumental *History of Economic Analysis* (1954), that there were remarkable economists among the mercantilists.

## 2. The latecomer central model

The latecomer central model characterized countries such as Germany, Italy, Sweden and the United States. The classic study of this development model comes from Alexander Gerschenkron (1962), who analysed European countries that developed in the latter half of the nineteenth century and found in them a larger degree of state intervention. These countries had to face the industrial imperialism of England and France, which, as Friedrich List (1999) put it in 1846, attempted to "kick the ladder" from under Germany.<sup>8</sup> In that country, the developmental state was called Bismarckian. The German industrial revolution, led by Otto von Bismarck (1815–1898), combined state intervention and investment banks and served as an example for other latecomer central countries. Hélio Jaguaribe, writing about Bismarckian development in 1962, noted that under it the domestic market was reserved to domestic industry and that the state played the role of an arbiter between conflicting forces.

Although the United States domestic market was also reserved to domestic manufacturers, the state's decisive role is not as clear because the liberal ideology was so prevalent there that the state's role in the country's industrialization is systematically obscured. Its first Secretary of the Treasury, Alexander Hamilton, was not only one of the three great Federalist philosophers, but a developmental economist — indeed, the doyen of developmental economists. His classic "Report on Manufactures" (1791), on the need to protect American industry, launched a lasting and consistent policy of industrial promotion that only ended as late as 1939, when the United States finally lowered its customs tariffs, which had been very high until that point.<sup>9</sup> According to Paul Bairoch (1993, pp. 40 and 51), the average import tariff in the nineteenth century and until the 1930s ranged from 35% to 48%, making the country, in the words of this remarkable economic historian, "a bastion of protectionism". Ha-Joon Chang (2002a, pp. 24–32) provides additional data bearing this out. The present author's interpretation of tariffs so much higher than those of the United Kingdom and France, where they were lowered more than 100 years previously, is a developmental strategy that neutralized the country's Dutch disease.<sup>10</sup>

<sup>8</sup> The expression "ladder kicking" was originally employed by Friedrich List in 1846 to describe the behaviour of England, which sought to convince the Germans not to industrialize by using the arguments of classical liberal economics. The argument describes the current behaviour of rich countries vis-à-vis developing ones. Ha-Joon Chang (2002a) picked up the expression and applied it very capably and appositely.

<sup>9</sup> According to William A. Lovett, Alfred E. Eckes Jr. and Richard L. Brinkman (1999), the United States made 621 concessions in a 1938 agreement with the United Kingdom that added up to US\$ 457.8 million and represented 37% of the country's durable goods imports.

<sup>10</sup> The right way to neutralize Dutch disease (long-term overvaluation of the exchange rate because commodities can be successfully exported at a substantially stronger exchange rate than tradable industrial non-commodities) is to impose a variable retention on the prices of the commodities giving rise to it. High import tariffs only neutralize Dutch disease on the domestic market side, by increasing the price of imports, while multiple exchange-rate regimes may neutralize it on both the import and the export side.



The United States' extraordinary natural resources, including oil, resulted in long-term overvaluation of the exchange rate because these commodities could be profitably exported at a stronger exchange rate than manufactured goods. The tariffs, therefore, were not so much a "protectionist" system as a means to neutralize Dutch disease for the purposes of the domestic market.

### 3. The independent peripheral model

The third developmental state model, the independent peripheral model, has Japan as an exemplar. The Japanese were humiliated when they were forced to open up to trade with the West in 1854 under the threat of Commodore Perry's cannons.<sup>11</sup> The Meiji restoration of 1868 —the Japanese nationalist revolution that freed the country from the West's tutelage— was followed by a strategy of copying Western technology and institutions. Rapid industrialization occurred in the following 40 years, under the direct control of the Japanese state.<sup>12</sup> This was how technology was copied. The copying of institutions came from 1908 to 1910, with the decision to privatize companies in competitive industries. Thus, the former Samurai of the Tokugawa period, who took part in the Meiji Restoration in a military capacity, became first a middle class of bureaucrats and then, with privatization, businessmen. Privatization had no ideological import: the Japanese simply copied the Western institutional model, which, in the case of competitive companies, assigns the role of economic coordination to the market. Classic works on latecomer independent development include those by Alexandre Barbosa Lima (1973) and Chalmers Johnson (1982) on Japan, by Alice Amsden (1989) on South Korea and by Robert Wade (1990) on Taiwan. These books clearly show the impact of the state's intervention —or industrial policy— on firms. What they lack, with the partial exception of Robert Wade's, is an accurate analysis of the active macroeconomic policy these countries embraced. Each sought, first, to limit foreign borrowing and penetration of the domestic market by multinational companies and, second, to get macroeconomic prices right: the profit rate, the interest rate, the wage rate, the inflation rate and, above all, the exchange rate. In this effort, Asian policymakers had a major advantage over their Latin American counterparts: they did not export commodities and so did not have to neutralize Dutch disease. But neither were aware of the problem. Corden and Neary (1982) had already published their paper on Dutch disease, but it manifested itself as a problem only in boom times. Only after Bresser-Pereira's (2008) paper did it become clear that Dutch disease could also derive from a structural variable, namely Ricardian rents, and that it could be successfully neutralized by an export tax on commodities.<sup>13</sup>

Concerning this third model of industrialization, China also illustrates the metaphor of flying geese originally proposed by Kaname Akamatsu (1962) for the way Asian countries copied the Japanese model in waves: first came South Korea, Taiwan and Singapore, then Malaysia and Indonesia, then China and Vietnam.<sup>14</sup> China, having declined enormously under the West's industrial imperialism since

<sup>11</sup> By the West is meant the group of rich countries around the North Atlantic plus Australia, New Zealand, Japan and the three East Asian countries that caught up in the twentieth century: South Korea, Taiwan and Singapore. The West is therefore not a geographical concept. Its members make up the modern empire, under the leadership of the United States. These are countries that have in common high levels of knowledge and high wages that they attempt to protect along with the profits of their firms. They are militarily organized through NATO and their main economic instruments are the International Monetary Fund and the World Bank.

<sup>12</sup> Angus Maddison's data suggest that the Japanese industrial revolution happened at the time of the Second World War, but the ability of these data to detect industrial revolutions is limited. Japan was only able to attack Russia in 1905, China in 1936 and the United States in 1942 because it had already developed a powerful manufacturing industry.

<sup>13</sup> In a 1989 conference held in Tokyo by the Institute of Developing Economies, the natural resource-rich Latin American countries were compared with the natural resource-poor East Asian countries, but none of the economists used the Dutch disease model to explain why the East Asian countries continued to grow fast even as Latin America fell behind from 1980. The book on the conference is Fukuchi and Kagami (1990).

<sup>14</sup> In the case of South Korea, the Japanese model was imposed in the more than 30 years of Japanese colonial rule and maintained after the country's independence. As Atul Kohli (1999, p. 94) points out, by 1940 Korea was already a country with a "relatively high level of industrialization".

the mid-1800s, had its national and supposedly socialist revolution in 1949. The national revolution was completed by the industrial revolution, which was divided into two parts, the first from 1949 to 1978 under the leadership of Mao Zedong (1893–1976) and the second from 1989 to 2010 under Deng Xiaoping (1904–1997). Mao thought he was carrying out the first phase in the Chinese socialist revolution, when he was in fact carrying out the first phase of the capitalist revolution: with him at the helm, China asserted itself as a genuinely independent nation-state, educated its population and developed infrastructure and basic industry — activities that the state can typically conduct effectively and with reasonable efficiency. The second phase of the industrial revolution involved privatization and production diversification. As had happened in Japan, the competitive sector of the economy was privatized and left to the market while the state maintained political control, planned the non-competitive sector and executed an active macroeconomic policy to make sure that the five prices, and particularly the exchange rate, were correct. In this second phase, where the market takes on a strategic role, China experienced the most extraordinary economic development of all time, outstripping even Japan's earlier example and achieving an average yearly growth rate of 10% for 30 years.

#### 4. The national-dependent peripheral model

The fourth developmental state model, the national-dependent peripheral model, was not as successful. Countries in this group were developmental enough to achieve the industrial revolution, but unable to maintain rapid growth rates from 1980 onward. In Brazil, per capita income growth dropped from almost 4% a year during the industrial revolution (1930–1980) to 1.2% a year from 1981 to 2014. Much the same happened in Mexico. When analysing the two countries' developmentalism in this period, Ben Ross Schneider (1999, p. 278) found it to have four basic characteristics: state-dependent profits and investment, a developmental discourse dominated by the need to industrialize and the role of the state in fostering industrialization, the exclusion of the majority of the population, and a highly institutionalized public sector bureaucracy.<sup>15</sup> I would add a fifth characteristic to the foregoing: over-dependence on foreign borrowing, which ultimately financed consumption far more than investment and was the central cause of the crisis and demise of the developmental state — something that was definitely not a feature of East Asia's independent peripheral model. This saved the East Asian countries from the deep financial crisis produced by the foreign debt crisis of the 1980s, which interrupted growth in the Latin American countries even as the East Asian countries continued to grow fast.

The main analysts of national-dependent development were Raúl Prebisch, Celso Furtado, Osvaldo Sunkel, Aníbal Pinto, Hélio Jaguaribe and Ignácio Rangel, whose fundamental contributions emerged in the 1950s and 1960s. Classic developmentalism argued that the market could not ensure correct microeconomic pricing in developing countries, particularly in the early industrialization phase, and proposed industrial policy as a remedy. Fifty years on, the new developmentalism reserves a secondary but strategic place for industrial policy and argues that in developing countries (and to a lesser extent rich countries too) the market is incapable, above all, of setting correct macroeconomic prices: (i) a low base interest rate around which the central bank conducts monetary policy, (ii) a balanced exchange rate that makes manufacturing companies using state-of-the-art technology competitive, (iii) wages that grow with productivity so that (iv) inflation is kept under control and, last but not least, (v) a satisfactory rate of profit for manufacturing firms, motivating them to invest. The very existence of central banks is, indeed, an admission of this incapability. To achieve this, besides defending balanced fiscal and external accounts, the country must adopt an active exchange-rate policy involving structural or long-term

<sup>15</sup> Where the public bureaucracy is concerned, this view applies more to Mexico than to Brazil. In an essential book, Schneider (1991) showed that the Brazilian public bureaucracy was relatively informal but very professional.



measures.<sup>16</sup> Asian techno-bureaucrats did not have this theoretical framework to rely on, but had an impressive ability to pragmatically align measures to correct microeconomic prices through industrial policy with the maintenance of the right macroeconomic prices through active macroeconomic policy.

In the 2000s, the economic development literature formulated the concept of the “middle-income trap” to explain the loss of growth momentum in a whole set of countries that it dubbed middle-income, but whose range of per capita income levels in fact mixes two categories, pre-industrial and middle-income countries, the latter of which, in the opinion of the present author, have already carried out their industrial revolutions (Eichengreen, Park and Shin, 2014; Jankowska, Nagengast and Perea, 2012; Kharas and Kohli, 2011). What this literature found was the obvious: countries that grow at high rates (more than 4% a year, for example) for a relatively long period of time (such as five years) then experience a relatively large drop in growth rates (to below 2.5% a year, for example). Having identified those periods, which are common to radically different types of countries, the literature then attempts to use econometric studies to determine the cause of the slowdown and finds answers that are simply tautologies, such as “lack of industrial diversification” or “too high a growth rate”, or that are too generic, such as “insufficient investment in education”.

From 1980, indeed, growth rates plunged in countries with national-dependent developmental states, like Brazil and Mexico. But explaining this radical change requires new historical facts that the middle-income trap literature does not provide. Nor are they to be found in Schneider’s (1999) explanation, according to which the central difference between Latin American and East Asian countries was the less formal and less powerful bureaucracy of Latin America. This is not a new fact. Certainly a more professional bureaucracy with greater powers in the economic arena is to be preferred, but it is worth pointing out that Mexico’s and particularly Brazil’s public bureaucracies were strong enough to bring about industrialization before 1980, and there is no reason why they should have weakened thereafter. The two new historical facts that best explain the drop in Brazil’s and Mexico’s growth rates are the great foreign debt crisis of the 1980s and the West’s increased criticism of the developmental state since the adoption of neoliberalism as an ideology and its practical definition in the shape of the Washington Consensus. These two factors led to the abandonment of the developmental strategy near the end of that decade. The liberal state embraced neoliberal policies, ceased to neutralize Dutch disease (which afflicts the majority of these countries) and began growing slowly except during commodity boom periods such as the 2000s. Chile has been the exception, but it is worth mentioning that the country changed its economic policy after the crisis created by the neoliberal experience of 1981–1982, making it less liberal, and has consistently maintained a high rate of tax on copper, partially neutralizing its Dutch disease.<sup>17</sup>

## IV. The developmental state after the industrial revolution

We therefore have four models for the developmental state at the time countries carry out their industrial revolutions: the original central, latecomer central, independent peripheral and national-dependent peripheral models. What about after the industrial revolution? At this stage, a country’s economy liberalizes. Britain and France were liberal from the 1830s to the 1920s, albeit theirs was not a radical

<sup>16</sup> To neutralize the tendency towards cyclical and chronic overvaluation of the exchange rate, the new developmentalism proposes an export tax to neutralize Dutch disease and a rejection of three commonly applied policies: growth combined with foreign borrowing (“savings”), the use of an exchange-rate anchor to control inflation, and a high real interest rate around which the central bank manages its monetary policy.

<sup>17</sup> The tax on copper exports would fully neutralize Chile’s Dutch disease if its rate varied with the severity of the disease (that is, exchange-rate overvaluation), which varies in turn with international commodity prices.

economic liberalism. In the 30 golden years of capitalism after the Second World War, however, the fifth model of developmental state arose: the social welfare developmental state, involving a state that was both developmental and social democratic and a major class compromise, of which Przeworski (1985) produced the definitive study, allowing for a combination of growth and distribution.

However, an economic crisis in the 1970s paved the way for a contradictory economic liberalism, namely neoliberalism, a conservative ideology based on neoclassical economics and Austrian theory that endeavoured to carry out radical economic reforms that were supported by conservatives, even though their radical character made them incompatible with conservatism. The new state born out of this, the neoliberal state, was a radical attempt to go back to the liberal state of the nineteenth century. The attempt failed, however. First, it made no sense to return to an inferior model of the state. Second, capitalism had undergone extraordinary changes and become much more complex, so that it required more, not less, state coordination. Globalization retreated after the global financial crisis of 2008 and the collapse of neoliberalism and the state resumed a far greater role in rich countries, so that while their states may remain conservative, they are no longer neoliberal. However, this cannot be construed as a return to a developmental and social state like that in place after the Second World War. These countries are currently in a transition crisis where the conditions for strengthening the social state are not present. One cause of the advent of neoliberalism was the competition from developing countries that rich ones started to face as the former began exporting manufactured goods. This began in the 1970s and rose to new levels with the emergence of China in the 1990s. Now, together with the problem of migration to rich countries, competition from countries with access to cheap labour has been one of the root causes of the crisis of the social democratic state and the appearance of a nationalist far right in Europe.<sup>18</sup>

The market takes on a greater coordinating role once a country has become capitalist, but this is not to say that the state must cease to be developmental. As has just been seen, the golden years of capitalism were a second stage of developmentalism for the central original countries. Yet market coordination is more important in developed than in developing countries. The political explanation lies in rentiers' and financiers' clear preference for economic liberalism and the growing ideological hegemony of this social class in relation to productive entrepreneurs. The economic explanation lies in the increased economic diversity arising from economic development. As economic activities become more diversified relative to the level of diversity evinced by infrastructure and basic industry firms in the non-competitive sector, the market becomes more efficient than the state at coordinating the very numerous and diversified firms that then emerge. While it is relatively easy for the state to plan and coordinate infrastructure, and there is no prospect of the market doing it, the market is a more appropriate institution when it comes to coordinating diversified activities involving creativity and innovation. Therefore, it can be predicted that once a country's industrial revolution is complete, market-based coordination will gain ground on coordination by the state. But this is not to say that the developmental state disappears, as liberal economists would have it. Instead, the state's economic role changes. Now, the state's essential role in the economic domain is to create the general conditions that make competent enterprises in the country able to compete and willing to invest, which means getting the five macroeconomic prices right (the profit rate, the interest rate, the exchange rate, the wage rate and the inflation rate) — something the market certainly does not achieve, as can be seen from the recurring price and financial instability that characterizes unregulated markets— and planning and partially investing in infrastructure and basic industry, adopting a strategic industrial policy, fostering scientific and technological development, promoting reduction of economic inequality, defending the environment, which is a public asset, and of course guaranteeing property rights and contracts. Once the industrial revolution is complete, therefore, the state over time retreats fully from competitive industries and partially from non-competitive ones

<sup>18</sup> Regarding the costs to the United States from its trade with China, Autor, Dorn and Hanson (2016, p. 1) conclude that, in addition to high regional costs because of firms shutting down, “[a]t the national level, employment has fallen in U.S. industries more exposed to import competition, as expected, but offsetting employment gains in other industries have yet to materialize”.

(which means limiting public investment to around one fifth of total investment), because the market is better equipped to coordinate competitive activities. If it is a developmental state, though, it will continue to coordinate the monopolistic sector of the economy and conduct an active macroeconomic policy.<sup>19</sup>

The main problem facing developmental and liberal states alike is the political and economic competence of their rulers. Successful developmental states have always relied on republican-minded nationalist politicians and pragmatic economists who knew that their core job was to ensure economic stability and develop policies that contributed to their country's industrialization or productive sophistication. Such competent politicians and economists are not always to be found. Politicians often give in to the temptation of raising people's incomes without the required increase in production and indulging in economic populism, be it exchange-rate populism, whereby the country runs up large current account deficits, or fiscal populism, whereby the state runs up large public deficits. In either case, the result is increased consumption and indebtedness, whether domestic, foreign or both. It must not be imagined, though, that the liberal state avoids these problems. Exchange-rate populism is a more common practice in this model of state than in developmental states. The liberal politicians and economists who govern developing countries believe in the thesis, very dear to rich countries, that current account deficits are foreign savings which, added to domestic ones, increase the country's investment rate. They do not know or care that there is a high rate of substitution of foreign for domestic savings in developing countries, where the marginal propensity to consume is high. More broadly, and against all evidence, they believe that the market correctly sets the foreign exchange rate, so that the government should not intervene in it. In developmental states, on the other hand, even if there was until recently no theory legitimizing exchange-rate policy, pragmatic exchange-rate management policies are commonly adopted because developmental economists know that strategies based on industrialization depend on the foreign exchange rate.<sup>20</sup>

## V. Concluding remarks

In conclusion, economic development is a historical process of productivity and wage increases arising from the use of increasingly skilled or sophisticated labour in activities with greater value added per capita. It is the result of a coalition of classes that brings politicians and public bureaucrats into partnership with the businessmen responsible for investment and innovation. Within this framework, the developmental state has historically been and must continue to be the central development-oriented institution because it is the state that guarantees and regulates another equally fundamental institution: the market, a merely economic institution. The scope of the state is far greater. It is the instrument par excellence for the nation to attain the five major political objectives of modern societies: security, liberty, economic well-being, social justice and protection of the environment, objectives that must constantly be the subject of compromises or the principle of reasonability in the light of perceived or real short-run conflicts with each other. Economic development is necessarily the outcome of a national development strategy arising when a strong nation shows the ability to build an equally strong or capable developmental state. Nations only form and remain alive and strong when they are the product of a constantly renewed national agreement. If the social contract that binds them together is not sufficiently sound, if the social classes that form it do not maintain basic ties of solidarity when it comes to competing internationally, they will not stand as true nations, the country will be far more vulnerable to hegemonic Western thinking and the nation will lose strength, as Latin American countries did after the great crisis of the 1980s.

<sup>19</sup> Japan's industrialization in the late nineteenth century was almost entirely carried out by the state. Around 1910, however, a rapid and radical privatization process took place. In the case of Russia and China, their professedly socialist revolutions were in fact national and industrial; paradoxically, they were part of the capitalist revolution.

<sup>20</sup> This theory constitutes the new developmentalism and its developmental macroeconomics. See Bresser-Pereira, Oreiro and Marconi (2014).

The developmental state, which lies between the liberal state and statism, is a superior form of capitalist economic and political organization. It is a means whereby state and market coordination can be sensibly or pragmatically combined in capitalist economies. Several models of the developmental state have existed over the course of history, depending on whether its development was original or latecomer, central or peripheral, first- or second-wave. Every industrial revolution has taken place within the framework of developmental states, when a group of nationalist politicians have successfully formed a nation-state and industrialized. This phase is always dominated by the state, which manages to regulate a broad and comprehensive market, whereupon activities in the competitive sector of the economy, which are now more diverse and involve more creativity and innovation, can be advantageously coordinated by this market. But the state needs to and usually does remain developmental, because it is responsible for coordinating the non-competitive sector of infrastructure and basic industry, implementing an active macroeconomic policy (including an exchange-rate policy), reducing economic inequality and protecting the environment — a set of activities that the market cannot accomplish.

## Bibliography

- Akamatsu, K. (1962), “A historical pattern of economic growth in developing countries”, *The Developing Economies*, vol. 1, No. 1, Hoboken, Wiley.
- Amsden, A. (1989), *Asia's Next Giant: South Korea and Late Industrialization*, New York, Oxford University Press.
- Autor, D., D. Dorn and G. Hanson (2016), “The China shock: learning from labour market adjustment to large changes in trade”, *Annual Review of Economics*, vol. 8, No. 1, Annual Reviews [online] <https://www.annualreviews.org/doi/full/10.1146/annurev-economics-080315-015041>.
- Bairoch, P. (1993), *Economics and World History: Myths and Paradoxes*, Chicago, Chicago University Press.
- Barbosa Lima, A. (1973), *Japão: O Capital se Faz em Casa*, Rio de Janeiro, Paz e Terra.
- Bresser-Pereira, L. (2016), “Reflecting on new developmentalism and classical developmentalism”, *Review of Keynesian Economics*, vol. 4, No. 3, Cheltenham, Edward Elgar [online] <http://dx.doi.org/10.4337/roke.2016.03.07>.
- \_\_\_\_\_(2008), “The Dutch disease and its neutralization: a Ricardian approach”, *Brazilian Journal of Political Economy*, vol. 28, No. 1, Sao Paulo, Editora 34 [online] <http://dx.doi.org/10.1590/S0101-31572008000100003>.
- \_\_\_\_\_(1963), “O empresário industrial e a revolução brasileira”, *Revista de Administração de Empresas*, vol. 3, No. 8, Sao Paulo, Getulio Vargas Foundation/School of Business Administration of Sao Paulo [online] [http://www.scielo.br/scielo.php?script=sci\\_arttext&pid=S0034-75901963000300001](http://www.scielo.br/scielo.php?script=sci_arttext&pid=S0034-75901963000300001).
- Bresser-Pereira, L. and M. Iannoni (2017), “Developmental class coalitions: historical experiences and prospects”, *Growth, Crisis and Democracy: The Political Economy of Social Coalitions and Policy Regime Change*, H. Magara and B. Amable (eds.), London, Routledge.
- Bresser-Pereira, L., J. Oreiro and N. Marconi (2014), *Developmental Macroeconomics: New Developmentalism as a Growth Strategy*, London, Routledge.
- Canitrot, A. (1975), “La experiencia populista de redistribución de ingresos”, *Desarrollo Económico*, vol. 15, No. 59, Buenos Aires, Institute of Economic and Social Development.
- Chang, H. (2002a), *Kicking Away the Ladder*, London, Anthem Press.
- \_\_\_\_\_(2002b), “The East Asian model of economic policy”, *Models of Capitalism: Lessons for Latin America*, E. Huber (ed.), University Park, Pennsylvania, Pennsylvania State University Press.
- Corden, W. and J. Neary (1982), “Booming sector and de-industrialization in a small open economy”, *The Economic Journal*, vol. 92, No. 368, Hoboken, Wiley.
- Díaz-Alejandro, C. (1981), “Southern Cone stabilization plans”, *Economic Stabilization in Developing Countries*, W. Cline and S. Weintraub (orgs.), Washington, D.C., The Brookings Institution.
- Eichengreen, B., D. Park and K. Shin (2014), “Growth slowdowns redux”, *Japan and the World Economy*, vol. 32, Amsterdam, Elsevier [online] <http://doi.org/10.1016/j.japwor.2014.07.003>.
- Evans, P. (1995), *Embedded Autonomy: States and Industrial Transformation*, Princeton, Princeton University Press.
- \_\_\_\_\_(1992), “The State as problem and solution: predation, embedded autonomy, and structural change”, *The Politics of Economic Adjustment: International Constraints, Distributive Conflicts and the State*, S. Haggard and R. Kaufman (eds.), Princeton, Princeton University Press.

- Fonseca, P. (2014), "Desenvolvimentismo: a construção do conceito", *Presente e Futuro do Desenvolvimento Brasileiro*, A. Calixtre, A. Biancarelli and M. Cintra (eds.), Brasília, Institute of Applied Economic Research (IPEA).
- Fukuchi, T. and M. Kagami (eds.) (1990), *Perspectives on the Pacific Basin Economy: A Comparison of Asia and Latin America*, Tokyo, Institute of Developing Economies.
- Gellner, E. (1996), "The coming of nationalism and its interpretation: the myths of nation and class", *Mapping the Nation*, G. Balakrishnan (ed.), London, Verso.
- \_\_\_\_\_(1983), *Nations and Nationalism*, Ithaca, Cornell University Press.
- Gerschenkron, A. (1962), *Economic Backwardness in Historical Perspective: A Book of Essays*, New York, Praeger.
- Hamilton, A. (1791), "Report on manufactures" [online] <http://bit.ly/1FaVTTg>.
- Ianoni, M. (2014), "Teoria do Estado desenvolvimentista: uma revisão da literatura", *Sinais Sociais*, vol. 9, No. 24, Rio de Janeiro, Departamento Nacional de Serviço Social do Comércio (SESC) [online] <http://bit.ly/2od6pYO>.
- Jaguaribe, H. (1962), *Desenvolvimento Econômico e Desenvolvimento Político*, Rio de Janeiro, Fundo de Cultura.
- Jankowska, A., A. Nagengast and J. Perea (2012), "The middle-income trap: comparing Asian and Latin American experiences", *OECD Development Centre's Policy Insights*, No. 96, Paris, Organization for Economic Cooperation and Development (OECD) [online] <http://dx.doi.org/10.1787/5k8x7gwqslp-en>.
- Johnson, C. (1999), "The developmental State: odyssey of a concept", *The Developmental State*, M. Woo-Cumings (ed.), Ithaca, Cornell University Press.
- \_\_\_\_\_(1982), *MITI and the Japanese Miracle*, Stanford, Stanford University Press.
- Kharas, H. and H. Kohli (2011), "What is the middle-income trap, why do countries fall into it, and how can it be avoided?", *Global Journal of Emerging Market Economies*, vol. 3, No. 3, Thousand Oaks, SAGE [online] <https://doi.org/10.1177/097491011100300302>.
- Kohli, A. (2012), "Coping with globalization: Asian versus Latin American strategies of development, 1980–2010", *Brazilian Journal of Political Economy*, vol. 32, No. 4, Sao Paulo, Editora 34 [online] <http://dx.doi.org/10.1590/S0101-31572012000400001>.
- \_\_\_\_\_(1999), "Where do high growth political economies come from? The Japanese lineage of Korea's 'developmental State'", *The Developmental State*, M. Woo-Cumings (ed.), Ithaca, Cornell University Press.
- List, F. (1999), *National System of Political Economy*, Roseville, Dry Bones Press.
- Lovett, W., A. Eckes Jr. and R. Brinkman (1999), *US Trade Policy: History, Theory, and the WTO*, Armonk, New York, M. E. Sharpe.
- Maddison, A. (1977), "Phases of Capitalist Development", *PSL Quarterly Review*, vol. 30, No. 121, Roma, Banca Nazionale del Lavoro.
- Przeworski, A. (1985), *Capitalism and Social Democracy*, Cambridge, Massachusetts, Cambridge University Press.
- Schneider, B. (1999), "The desarrollista State in Brazil and México", *The Developmental State*, M. Woo-Cumings (ed.), Ithaca, Cornell University Press.
- \_\_\_\_\_(1991), *Politics within the State: Elite Bureaucrats and Industrial Policy in Brazil*, Pittsburgh, Pittsburgh University Press.
- Schumpeter, J. (1954), *History of Economic Analysis*, London, Allen & Unwin.
- Wade, R. (1990), *Governing the Market*, Princeton, Princeton University Press.
- Woo-Cumings, M. (ed.) (1999), *The Developmental State*, Ithaca, Cornell University Press.