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THE INTERNATIONAL POLITICAL ECONOMY AND THE DEVELOPING COUNTRIES

VOLUME I

Stephan Haggard

The International Political Economy and the Developing Countries Volume I

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Introduction

I

The study of the developing countries in the international political economy has rotated around three closely related debates. By far the most central concerns the effects of the international system on the developing countries. On one side is the liberal intellectual tradition in economics running from Ricardo to neoclassical trade and growth theory, and including the modernization theorists in sociology and political science. This tradition emphasizes the net benefits for developing countries of integration into the world economy, with those benefits defined primarily in terms of efficiency and aggregate economic growth. Inextricably intertwined with this positive argument are two normative ones: that developing countries should pursue development strategies based on the exploitation of their comparative advantage and, more controversially, that the best way of achieving this objective is through policies of free trade and capital flows.

Much theoretical work in this vein has been devoted to reiterating the general findings of neoclassical trade theory and arguing that those laws applied equally well to developing countries. Though there were voices making such arguments throughout the 1950s and 1960s, the neoclassical revival in development economics did not gain steam until the 1970s.

The liberal tradition never paid much attention to the crucial question of why developing countries failed to pursue optimal policies. 'Nationalism' and 'ideology' were favourite, if unsatisfying, answers to this question until the emergence of the literature on rent-seeking. Despite the popularity of the concept, however, economists did surprisingly little empirical work on rent-seeking; the phenomenon was frequently invoked but rarely tested. This left the field to political scientists, and over the 1970s and 1980s a rich literature developed on the political and institutional determinants of different development strategies.

An alternative to the rent-seeking explanation of why developing countries failed to pursue optimal policies was that the policies recommended by neoclassical theory were not, in fact, optimal. A diverse set of competing intellectual traditions – nationalists, Marxists, Keynesians, dependistas, world systems theorists and realists – emphasized the negative sociological and political, as well as economic, effects of integration into the world economy. Naturally, a quite different set of policy prescriptions followed. First and foremost, policies based on the pursuit of comparative advantage, including through relatively open commercial policy, implied permanent consignment to 'peripheral' status. It followed that the state should be centrally involved in the process of economic development: through planning, by controlling international exchanges, and through bargaining with foreign actors and governments.

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Finally, this approach argued that developing countries needed to exploit their collective power – such as it was – to change the international regimes governing economic exchange. The critical stance towards integration into the world economy served as the basis for periodic political movements aimed at altering – or overthrowing – the existing international order. Economic arguments were central to nationalist movements struggling against imperial dominance. In the post-independence period, a critical view of North–South economic relations undergirded regional integration efforts, the non-aligned movement, and the quest for preferential treatment within the GATT system. These ideas also influenced the ambitious agenda of the New International Economic Order (NIEO) that arose in the 1970s. The NIEO was crucial in breathing life into the study of 'North–South' relationships, but disappeared virtually without a trace in the crisis-ridden decade of the 1980s.

This central debate on the integration of developing countries overlaps with a second controversy concerning the extent and effects of international power differences. The very division of the globe into 'developing' and 'developed', 'backward' and 'advanced', implies asymmetry. How much does such asymmetry matter to the welfare of developing countries?

The lines in this second debate do not overlap clearly with those in the first. The liberal tradition remains uncomfortable with the concept of power and is inclined to discount the effects of asymmetries on the grounds that exchange relations are positive sum games. Bargaining theorists underlined ambiguities in the concept of 'power', and noted that traditional measures were not very good predictors of bargaining outcomes. There were a variety of strategies that developing countries could use to advance their interests successfully, even in the face of apparently large power differences.

Both realists and structuralists were more sceptical. As long as power asymmetries between developed and developing states remained, empire and imperialism would constitute facts of international life. Even in the absence of overt political control, asymmetries in power would dictate bargaining outcomes, not only between states, but between developing countries and transnational actors as well.

The third, related, controversy centred on how developing countries should be studied. Traditionally, the field of comparative politics assumed that individual countries could be studied as discrete units. Dependency, world systems theory and what might be called 'open-economy political economy' changed that view irrevocably. By showing the ubiquitous influence of international markets and politics on domestic outcomes, these theoretical developments effectively erased the boundaries between comparative and international political economy. No serious study of the developing countries is now possible without reference to the international economic setting. Conversely, the study of the 'international' political economy of the developing countries must refer back to the domestic coalitional and institutional underpinnings of external economic relationships.

II

Selecting the major works on the international political economy of the developing countries has posed a number of challenges and difficult decisions. Should such a collection concentrate on works conforming to a particular intellectual style – such as positive political economy – or should it reflect the intellectual and disciplinary diversity that has characterized writing on North–South relationships? What weight should be given to older work as compared to recent scholarship? Should works be admitted to the canon if they were once influential but have been superseded since? What weight should be given to general theory, as opposed to the analysis of particular issues areas such as trade and investment? And how should the balance be struck between the different disciplines that have addressed the issue: history, economics, political science and sociology?

I have chosen pieces of three sorts. First, I have included 'classics' that had strong influence on subsequent debate; even if not all of these have held up well, they are important for reasons of the sociology of knowledge. Secondly, I have chosen a handful of pieces that are exemplary of a particular theoretical and research tradition, even if they are somewhat less well known. Finally, I have included several review essays that provide overviews of important lines of thinking; in some cases the review essays are more incisive than the literature they survey.

For reasons of space, I have steered clear of work which, while of obvious relevance to the developing countries, was not formulated with specific reference to them. Examples include the Stolper/Samuelson formulation of neoclassical trade theory and Vernon's initial exposition of the product cycle model of international investment; these pieces are contained in the trade and foreign investment volumes of this project respectively.

Volume I contains broad theoretical or empirical statements that have relevance across a range of functional issue areas. Volume II looks at four discrete issue areas – trade, foreign direct investment, aid and debt – and the issue of the international regimes of relevance to the developing countries.

III

The early post-war analysis of the developing countries by economists was surprisingly sceptical about the benefits of free trade and capital movements; the liberal pole of the first great debate outlined above was generally in retreat. This scepticism reflected the experience of the Great Depression, the spread of Keynesian ideas, the lure of planning and a concern about the export prospects of developing countries in the face of a secular decline in the terms of trade. Rosenstein-Rodan's influential article on the problems of Eastern Europe was a precursor of what was to follow. The evidence on the terms of trade was spelled out in an important article by W.A. Lewis, though it later became clear that his findings were flawed in important respects. Seminal pieces by Hans Singer and Raul Prebisch approached the question theoretically, providing the justification for the critique of close integration into the world economy and for the strategy of import-substitution industrialization (ISI).

The Lewis essay on 'Economic Development with Unlimited Supplies of Labour' was not formulated with particular reference to the question of trade, but its influence on the analysis of the international position of the developing countries was immense. By emphasizing the dualistic structure of labour markets – and the structure of production more generally – it provided a model of why the developing countries were fundamentally different from their advanced country counterparts. This idea remains central to virtually all work in the development field to this day, and was particularly important to dependency theory.

Part II of Volume I provides seminal examples of the critical literature on the political economy of underdevelopment that emerged in the 1960s and 1970s. This work was hostile to liberalism, and emphasized the importance of power and imperialism in the analysis of developing countries. Though this literature had antecedents in the work of Rosenstein-Rodan, Singer, Prebisch and other economists, as well as in the Marxist literature on imperialism, the most important post-war precursor was undoubtedly Paul Baran. Baran's 1952 article, 'On the Political Economy of Backwardness', expanded in his book entitled *The Political Economy of Growth*, was one of the first political economy treatments of the subject.

The stark and simple dependency model of André Gunder Frank became an easy target for critics, but Frank's work was highly influential and triggered a new round of theory and research. Frank's most lasting contribution was not so much theoretical as methodological. Post-Gunder Frank, it was impossible to study the developing countries as isolated units without reference to the international systemic context.

Early dependency theory spawned several progeny. Wallerstein's world-systems approach pushed the dependency project to its logical conclusion; the short contribution included here summarizes Wallerstein's complex work. He argued that except for isolated subsistence communities, all economies – core, 'semi-peripheral' and peripheral – were part of a single world system, and that that system had to be studied as a totality. Hierarchy and the exercise of both state power and economic power through 'commodity chains' were central to Wallerstein's conception of the international system.

Like the idea of a 'semi-periphery' in Wallerstein's work, the concept of 'dependent development' grew out of the embarrassing observation that the periphery – assigned by Frank to more or less permanent stagnation – was, in fact, growing rapidly. Moreover, it appeared that this growth was being fuelled precisely by close integration into the world economy, particularly through the mechanism of foreign direct investment. Cardoso's 'dependent development' approach sought to study the nature of this growth, but remained squarely within a critical vein by emphasizing the negative political, sociological and economic consequences of dependency, including authoritarianism, inequality and dualistic economies.

The dependency and dependent-development approaches had tremendous influence on North American social science, particularly in the field of Latin American studies. Peter Evans's influential book *Dependent Development* followed in Cardoso's theoretical path, but added careful sectoral studies of the political economy of foreign direct investment (see Volume II, Chapter 7). Christopher Chase-Dunn, a sociologist, pioneered cross-national quantitative studies of dependency, focusing particularly on the issue of the international systemic determinants of inequality.

Criticism of dependency theory often exhibited the worst features of the academy: the most crude versions of the model were set up for attack, while the more nuanced versions of the approach and its larger contribution were downplayed. Nonetheless, some criticisms advanced the debate. Kaufman, Chernotsky and Geller offered one of the first quantitative tests of dependency theory. Though they did not cast their arguments explicitly in terms of mainstream economic theory, their findings suggested that the relationship between dependency and growth was positive, as the liberals had long claimed. Smith offers the most wide-ranging criticism from the perspective of mainstream political science, emphasizing definitional and methodological weaknesses in dependency writing.

Bill Warren's essay, by contrast, offers a stinging indictment of dependency theory from the left. Warren argued that Lenin's theory of imperialism, which first suggested that the penetration of capitalism into the periphery could have negative economic consequences, was untrue to Marx. Rather, Marx saw the global spread of capitalism as a progressive force. Warren marshalled evidence that those developing countries most closely integrated into the world economy were the ones growing most rapidly.

The third theoretical section in Volume I includes writing from what I call the 'neoclassical revival' that began in the 1960s but gained steam in the 1970s and 1980s. There were a few lonely voices who articulated the liberal case for the developing countries in the 1950s and early 1960s, but their claims did not gain wide resonance until later. Three developments explain the re-emergence of liberalism in the guise of the extension of neoclassical economic theory to the Third World.

First, the negative effects of import substitution became increasingly apparent over time. A balanced and typically wise review of the early literature is provided by Carlos Díaz-Alejandro, whose premature and tragic death was a great loss to the field. Krueger's famous essay on rent-seeking approached the problem of import substitution from a formal political economy perspective. Krueger's essay had implications far beyond the developing countries, but it grew directly out of her long-standing work on development and exercised tremendous influence on how economists thought about the political economy of ISI.

The second development that buttressed the neoclassical cause was the success of the East Asian newly industrializing countries. A growing number of comparative studies vindicated classical liberal prescriptions by providing evidence that 'outward-oriented' growth strategies were superior to 'inward-looking' ones. Balassa's essay summarizes his prolific engagement with the issue (and contains a useful bibliography of his work).

The neoclassical interpretation of East Asia's growth did not go unchallenged, however. In an influential book, Robert Wade argues that export-led growth was a mercantilist strategy. Though the East Asian countries pursued an outward-looking strategy, this strategy should not be conflated with a liberal one. Markets in Korea, Taiwan and Japan remained relatively closed, and export success came about as a result of industrial policy and subsidies; in short, through extensive state intervention in the market.

A third development that gave weight to the neoclassical revival was the debt crisis, examined in more detail below. The crushing balance-of-payments crises experienced by the major debtors in the 1980s were interpreted as but another manifestation of the weakness of inward-oriented growth strategies. John Williamson's contribution outlines what he dubbed the 'Washington consensus', a codification of the policy reforms favoured by the World Bank, the IMF and the dominant development policy community in the advanced industrial states.

The neoclassical revival was primarily occupied with the normative issue of what development strategies were optimal. From a positive political economy perspective, however, the important question was to account for the alternative growth strategies that countries pursued. The range of domestic political factors that might plausibly influence governments' strategic choices is extremely wide, however, and includes underlying social coalitions, political institutions and ideology; some diverse examples of this important new area of research are included in Part IV of Volume I.

One puzzle centres on explaining the rise of import-substituting strategies. Albert Hirschman drew on economic theory to emphasize how import-substitution policies affected the interests of different sectors. Robert Bates also adopted a sectoral approach, using a simple rent-seeking and rent-supplying model to explain the weakness of agricultural exporters in Africa; his work proved immensely influential. Maxfield and Nolt, by contrast, advance a sophisticated dependency analysis of import substitution, focusing their attention on the interests of American multinationals.

A second puzzle that has received increasing attention is the political economy of export-led growth in the East Asian newly industrializing countries. The theoretical framework provided by Ranis and Mahmood summarizes Ranis's influential stages model of growth, which places particular emphasis on resource endowment and international shocks as determinants of development strategy. Weakly endowed with natural resources, the Asian NICs were unable to finance extended periods of ISI; in the face of international shocks, they turned to exports. Jeffrey Sachs's comparison of growth strategies in East Asia and Latin America argues that the political weight of the agricultural sector was a factor behind the realistic exchange rate policies of the East Asian NICs, which in turn were one key to the region's success. Stephan Haggard reviews a range of political factors that affected the development of the East Asian and Latin American NICs, but places particular emphasis on the role of the state in the East Asian model; his work is complementary to the critique of neoclassical analysis offered by Wade.

IV

Volume II turns to examples of important theoretical work on the international political economy of four issue areas: trade, foreign direct investment, aid and debt. Each of these topics is immense, and several are covered elsewhere in this series. I have therefore been particularly selective, focusing on a handful of seminal or representative pieces that are of relevance to the great debates outlined above. I have therefore ignored much good work.

The export of primary commodities constituted the traditional role of the developing countries in the international system; it was discomfort with this role that formed the basis of the post-war critique of liberalism. Much of the dependency literature included already touches directly or indirectly on the problems of primary commodity export, including claims about declining terms of trade and the political control exercised by multinational corporations. The piece by Melville Watkins is useful because it outlines the *benefits* of staple exports, drawing on the experience of Canada.

At the international level, the main issue confronting the commodity producers was whether they could effectively organize to influence prices. Though tremendous political and intellectual energy was expended on the issue, Krasner makes a convincing argument that oil was the exception in this regard; the essay holds up well.

The developing countries' surprisingly rapid diversification into manufactured exports was a major source of the new protectionism in the advanced industrial states. Much of the literature on trade policy in the developed countries was, in effect, about the consequences of the emergence of Japan and the NICs as major exporters. At the international level, the crucial issue was the extent to which protection constrained the developing countries. Yoffie was one of the first political scientists to write on the topic. He showed that the use of quantitative restraints was not as restrictive as might have been expected, and that LDC exporters had numerous strategies for circumventing or limiting the effects of the new protection.

In part because it became a preoccupation of dependency writing, the literature on the political economy of foreign direct investment in the developing countries has generally been deeper than that on trade. The debate about foreign investment mirrored closely two of the big controversies outlined above: the question of the economic, social and political effects of integration into the world economy, in this case through foreign investment; and the issue of how much power and bargaining leverage the developing countries had *vis-à-vis* the multinationals.

The question of bargaining power and the distribution of gains was first posed by Edith Penrose in her seminal 1959 article. In the 1970s, a new bargaining school emerged as a critique of dependency analysis. The bargaining school argued that the dependency approach was overly deterministic and that developing countries maintained a variety of strategies that could shift particular bargains in their favour. Grieco provides a summary of the debate. A particularly nuanced example of such bargaining work is Shafer's piece on African efforts to capture the mining multinationals, which stresses the political disadvantages of nationalization.

Peter Evans's influential book on dependent development in Brazil initiated a new round of research on the multinational corporation. Evans drew not only on theories of imperialism, but on theories of foreign investment that emphasized industrial organization and the oligopolistic structure of the markets in which MNCs operated. The essay with Gary Gereffi raises these questions, but goes beyond the debate on bargaining and dependency to the determinants of different development trajectories.

Newfarmer's essay marks the theoretical highpoint of the dependency literature. By attempting a synthesis of the industrial organization and dependency approaches, Newfarmer is able to give greater precision to dependency claims about the power of the multinationals. This promising approach to the question of power in North–South relations has still not been fully exploited.

Many of the dependency and bargaining studies took the form of case studies of particular industries and countries. Yet several excellent studies took a cross-national quantitative approach, with good effect. The essay by David Jodice, included here, is exemplary.

A number of empirical studies have provided detailed analysis of various aspects of foreign aid, but few explicitly attempted to model the process. The essay by Mosley focuses on the conditionality of the international financial institutions, a topic that spawned a vast literature following the debt crisis of the 1980s. What is distinctive, however, is Mosley's effort to provide a simple, schematic treatment of the underlying dynamics of the aid relationship.

As the political economy of Third World debt is not covered elsewhere in this series, I have given it somewhat greater attention than the literature on trade and foreign investment. The articles by Frieden and Lipson were among the first to address the political economy of the debt crisis. Frieden highlighted the domestic politics of the debt-led growth strategy of the 1970s. Lipson outlined the structure of the 'debt regime' circa 1980, emphasizing the central role of the multilateral institutions. Eaton and Taylor review the early work on debt by economists. This literature addressed central issues in political economy, including the role of strategic interaction in the credit markets and the particular problems posed by sovereign risk.

By the middle of the decade, the focus of attention shifted to the political economy of the adjustment process. As with the literature on the political economy of development strategies, the range of analytic approaches to the politics of adjustment was as wide as the field of comparative politics itself. Joan Nelson's article was one of the first to review the range of factors that affect the politics of stabilization. Frieden outlines a sectoral model of the politics of adjustment in Latin America. The contribution by Berg and Sachs, which focuses primarily on the effects of income inequality, represents one of the first attempts by economists to address the political economy of adjustment.

The debate on the adjustment process was not limited to political economy questions. There was also the crucial normative issue of whether the orthodox adjustment strategies (as outlined by Williamson in Volume I) were desirable.

The final section examines how the rules governing the international system affect the prospects of the developing countries. One pattern of international organization favoured by Prebisch and other early developmentalists was regional integration. A large literature on this subject developed in political science, but the article by Lynn Mytelka is the sharpest statement of why such schemes tended to fail. The passage of the NAFTA and the resurgence of regional integration efforts among developing countries will no doubt revive interest in this issue in the future.

The 1970s were characterized by an extensive debate on the possibility of establishing a new international economic order. Kreinin and Finger cast a sceptical eye on the NIEO programme, and Krasner offers an explanation of why the developing countries wanted the programme they did. We have fewer comparable studies of the developing countries in the international trade regime in the 1980s.

V

As can be seen from this review, the study of the developing countries in the international political economy has been driven both by changes in intellectual fashion and developments in the real world. The debate about the advantages of integration with the international system has swung through several phases, and the differences between the protagonists have narrowed. It is clear that the quest for self-reliance was misguided and costly in many instances and that some form of engagement with the international economy is a necessity for developing countries. Yet several important questions remain.

At the international level, there is the issue of how, precisely, the developing countries will be politically integrated into the international economy. Several scenarios are possible; each raises important research questions for the future. One possibility is that the developing countries – or the upper tier ones at least – will gradually come to assume full obligations in the multilateral system. As this occurs, the role of the developing countries in international trade negotiations is likely to become a more interesting topic for investigation than it has been in the past. New issues such as services, intellectual property and trade-related investment measures are of central concern to developing countries.

A second possibility is regionalism. The debate about regional blocs, including those that span the North–South divide, constitutes a central research topic. To date, much of the interest has been in the conflict among such blocs. A topic of equal interest is how such blocs might be structured internally; research on the NAFTA and on US commercial diplomacy in the Western hemisphere, on Japan in East and South East Asia, and on the evolution of the EC's relationships with its client states is likely to yield answers.

A third area for research is the continuing role of bilateralism in North–South relations. Power and bargaining models are still of relevance for understanding the increasing pressure on the developing countries for economic reform.

There is also the question of how the developing countries will be economically integrated into the international system. One issue that is likely to witness a revival of research attention is the study of foreign direct investment. The relationship between trade and investment is becoming increasingly close, and the full implications of a world trading-system increasingly structured by multinational firms, including multinationals from the developing countries themselves, has yet to be fully grasped. One promising line of research will be to extend the insights of the literature on industrial organization to an analysis of the firms, networks and commodity chains that link North and South.

At the domestic level, it is still premature to declare the triumph of liberalism. The East Asian countries still constitute a profound intellectual challenge, and suggest that there are alternative forms of capitalism that the developing countries might emulate. We still don't know theoretically why the East Asian model has worked, or whether it is replicable in other developing regions. Nor do we understand fully how the process of liberalization will unfold in other regions, and whether the reforms that are sweeping South Asia, Africa and Latin America are in fact politically durable.

Methodologically, the greatest pay-off for tackling these questions continues to lie with closer integration of the study of domestic and international political economy, an observation that we owe in no small measure to the dependency tradition. Yet precisely how to do this remains elusive. Part of the problem is how to integrate into one model a discussion of international and domestic processes which usually occur simultaneously. A revival of dependency approaches which focus on transnational coalitions might provide one solution to this problem of two-level games.

An even larger problem, however, is that the range of possible approaches to the domestic politics of foreign economic policy is virtually limitless. Nonetheless, some directions are emerging. Through closer attention to the economics literature, political scientists are gaining a better understanding of how sectoral interests affect preferences with regard to foreign economic policy; indeed, this work has become relatively straightforward. But we know much less about how such preferences are aggregated through institutions. In this important respect, certain key puzzles with regard to the international political economy of the developing countries will have to await advances in comparative politics.

Stephan Haggard