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Guest Contributor

Michael Spence

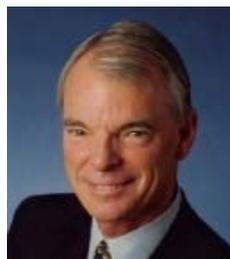
Professor of Economics at the Stern School of Business at New York University, Professor Emeritus of Management in the Graduate School of Business at Stanford University, a Senior Fellow of the Hoover Institution at Stanford and a Distinguished Visiting Fellow of the Council on Foreign Relations and Chair of the Academic Board of the Fung Global Institute.

Research & Development

Michelle Noguichi

On 30 January 2012 The Evian Group @ IMD welcomed Nobel Laureate Michael Spence for an evening discussion about his recently released book, *The Next Convergence*. IMD alumni, Corporate Learning Network members and PED program participants joined The Evian Group network to learn from Spence's far-reaching and incisive perspectives on "the future of economic growth in a multispeed world." The following morning, Spence presented and met with IMD MBA students as part of The Evian Group's Annual MBA Roundtable, which this year focused on "equity and sustainability" and engaged a host of world-renowned experts to discuss the challenges globalization presents, from poverty to gender to climate change.

A Discussion with Nobel Laureate Michael Spence



In his opening remarks, IMD Professor Jean-Pierre Lehmann described Spence as a rare breed – a "modest economist" who has demonstrated that economics originated in moral philosophy, prior to its shift into a more mathematics-focused discipline. Among Spence's many career accomplishments, Professor Lehmann detailed two that have distinguished him and provide a backdrop to his approach to world economics order in *The Next Convergence*.

The Sveriges Riksbank Prize in Economic Sciences in Memory of Alfred Nobel, 2001

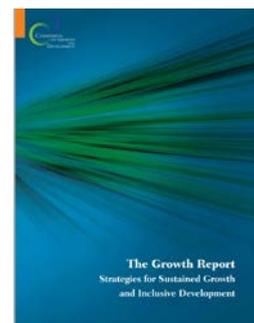
In 2001 the Royal Swedish Academy of Sciences awarded the Bank of Sweden's Sveriges Riksbank Prize in Economic Sciences in Memory of Alfred Nobel jointly to George A. Akerlof, University of California at Berkeley, A. Michael Spence, Stanford University, and Joseph E. Stiglitz, Columbia University, USA "for their analyses of markets with asymmetric information." In summary, "this work defined how many markets are characterized by asymmetric information, i.e. one side of the market having better information than the other, e.g. borrowers knowing more than lenders about their repayment prospects, managers and boards knowing more than shareholders about the firm's profitability, and prospective clients knowing more than insurance companies about their accident risk. Spence laid the foundation for a general theory of markets with asymmetric information, forming the core

of modern information economics. He identified an important form of adjustment by individual market participants, where the better informed take costly actions in an attempt to improve their market outcomes by credibly transmitting information to the poorly informed. Spence demonstrated when such signaling will actually work."¹

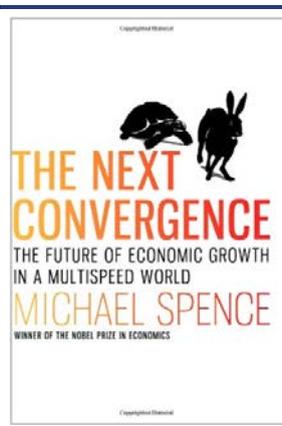
Chair of The Commission on Growth and Development, 2006–2010

In 2006 the Commission on Growth and Development was formed to bring together leading practitioners across sectors – from government, business and policymaking – mostly from the developing world. The Commission's goal was to understand the policies and strategies that enable rapid and sustained economic growth and poverty reduction. In *The Growth Report: Strategies for Sustained Growth and Inclusive Development*, the Commission was successful in detailing that fast, sustained growth is both possible and predictable.

Developing countries that combine the right approach (incentives, public investment and diversification) with strong leadership can and do leverage opportunities that the global economy affords. These findings laid the foundation for Spence's book *The Next Convergence: The Future of Economic Growth in a Multispeed World*.



¹ "The Sveriges Riksbank Prize in Economic Sciences in Memory of Alfred Nobel 2001." Nobelprize.org, <www.nobelprize.org/nobel_prizes/economics/laureates/2001/#> (accessed 27 March 2012).



Michael Spence has written an intelligent, rational and humane book about the great economic event of our era: convergence, or the rapid rise of once poor countries. Anyone seeking a common-sense guide to the transformation under way need look no further.

Martin Wolf, "Review: *The Next Convergence*." *FT.com*, 20 June 2011.

The Next Convergence? What is it?

The recent period of growth in developing countries has resulted in their convergence with established countries. Spence details how the global economy will evolve over the next fifty years, and puts into perspective how economic growth can be sustained in both advanced and developing countries, thus reshaping the world economy and favorably benefitting the many versus the few. Post World War II, a reversal of the past 200 years of divergence has occurred. The world is now almost midway through a century of convergence, and Spence provides a comprehensive "tour of critical parts of the world economy," detailing the scale and complexity of this redefining period.

Where has growth been achieved?

Out of about 180 countries in the world, 13 have grown at an average rate of 7% or more for 25 years. While not a long list, this is a remarkable achievement that would not have been thought possible 50 years ago.

Needless to say, the scale and velocity of this growth have dramatic impact, especially on the poor. "Growth with a reasonably inclusive pattern of the distribution of benefits is a potent weapon in reducing poverty."²

Why have these countries achieved sustained growth?

While Spence outlined a number of criteria, he profiled the following during his talk:

1. Openness to the global economy
2. Inclusiveness and equity
3. Leadership, especially at the national level.

Openness to the global economy – critical!

As Spence explained, there are "no barriers or market limits for a small, poor country." When supported by flows in capital, transfers of knowledge and technology, a nation creates the capacity for growth. However, this is still only one of several requirements for creating and sustaining growth.

Economy	Period of high growth [†]	Per capita income at the beginning and in 2005 [‡]	
Botswana	1960–2005	210	3,800
Brazil	1950–1980	960	4,000
China	1961–2005	105	1,400
Hong Kong*	1960–1997	3,100	29,900
Indonesia	1966–1997	200	900
Japan*	1950–1983	3,500	39,600
Korea, Rep. of*	1960–2001	1,100	13,200
Malaysia	1967–1997	790	4,400
Malta*	1963–1994	1,100	9,600
Oman	1960–1999	950	9,000
Singapore*	1967–2002	2,200	25,400
Taiwan*	1965–2002	1,500	16,400
Thailand	1960–1997	330	2,400

*Economies that have reached industrialized countries' per capita income levels.

[†]GDP growth of 7% per year or more.

[‡]In constant US dollars of 2000.

Source: World Bank. World Development Indicators

² Spence, Michael, *The Next Convergence: The Future of Economic Growth in a Multispeed World*. New York, NY: Farrar, Straus and Giroux, 2011, p. 55.

Inclusiveness and equity

This combination, according to Spence, is “not a nice add on, but inherently important to growth strategy. If you goof on this one, you won’t grow.” Inclusiveness in economics originated in India, but it is now broadly used and relates to how growth is distributed. The notion of inclusive growth is widely debated and a single definition does not exist. For Spence, it means “that people should not be left out or excluded from the opportunities created by growth, and there should be no limits to the amount of inequality in income and access to basic services that are tolerable.”³ In the absence of inclusiveness and in extremes of inequality, societal and political challenges to growth will emerge.

Leadership

Spence stressed, “Having a vision and being able to build consensus is critical again.” Top leadership at the national level, who recognize that growth will take compromise and sacrifice, is key during the start-up phase. Once growth strategies begin to gain traction and lead to successes, effective governance and strong institutional infrastructures need to be built up over time. As this occurs, top leadership are on the hook, having to learn, make mistakes and evolve in a dynamic

environment or trust and governance will erode quickly.

A Moral Community of Concern – Our Current Dilemma

In *The Growth Report*, Spence attempts to answer the key question: “Who do I care about? My immediate family, my extended family, neighborhood, region, the world?” In doing so, he examines the nature of equity and equality between nations, pinpointing both the philosophical and technical challenges arising from global policy instruments on responsibility.⁴

Convergence – “The rest of the world has joined the party!”

Having now reviewed what has passed, Spence turns his attention to the future. Will this fast growth continue and what is it reliant on? For the world economy to expand and grow in a more equitable way, he highlights three categories of concerns – instability and volatility, economy and demand, and the tension between nations and the globe (part to whole), especially as they relate to energy, environment, food and industrial composition. He illustrates these concerns by profiling three dominant economies – China, India and Brazil.

We chose to focus on growth because we think that it is a necessary condition for the achievement of a wide range of objectives that people and societies care about. One of them is obviously poverty reduction, but there are even deeper ones. Health, productive employment, the opportunity to be creative, all kinds of things that really matter to people seem to depend heavily on the availability of resources and income, so that they don't spend most of their time desperately trying to keep their families alive.

Michael Spence, during his tenure as Chair of the Commission on Growth and Development

When Does It Fail?

- Leadership
- Failures of governance
 - But the form of governance is not highly correlated with economic performance
- Pursuit of other objectives than growth
- Natural resource distortions of political
- National identity not formed
- Low rates of public sector investment
- “Bad,” meaning misguided strategy
- Inclusiveness failure

³ Spence, Michael, *The Next Convergence: The Future of Economic Growth in a Multispeed World*. New York, NY: Farrar, Straus and Giroux, 2011, p. 87.

⁴ *The Growth Report: Strategies for Sustained Growth and Inclusive Development*. Washington, DC: World Bank, Commission on Growth and Development, 2008. <www.growthcommission.org/index.php?option=com_content&task=view&id=96&Itemid=169> (accessed 27 March 2012).

I personally enjoyed Michael Spence's analysis of the current situation and his view of the mid-term future. I think we are moving from good to better worldwide. Historically speaking, it is an amazing time that we are living in. I often get bored in "lecture-type" presentations BUT, I found it was worth listening to Michael.

A participant

Spence then progresses through the consequential influencers to sustain growth, examining energy, climate change, information technology and global governance. In the end, the "long-term sustainability challenge" grabs significant real estate and focuses our attention on the global economy's explosion – slated to triple in the next 25 years, concentrate in Asia and necessitate change in individual, national and global patterns, models and behaviors. Academic, business and political elites have lost their luster. Spence acknowledges the mistakes made and that these do not seem to have engendered a more humble response to what this problem-solving requires, leaving a void which is currently being filled by political battles over aspirations that are not shared.

Conclusion

Spence leaves us with a deeper understanding and optimistic perspective of some of the critical influences and requirements to achieve a better world order. He describes the world in which his grandchildren will live as one that is made up of countries with 85% to 90% of their population earning high incomes (vs. 15% to 20% currently) and based on innovation (vs. one based on past experience and outdated policies and tools).

This world may well be beyond our imagination now, but we should not be daunted by it. He challenges us and the next generation to rise to the long-term growth and sustainability challenge with the confidence that our ingenuity will prevail. He does not sugarcoat this message; instead, he prepares us for a long and bumpy ride.

The Long Term Sustainability Challenge

- Global economy will triple in next 25 years
- Most of the growth in absolute terms will be in Asia
- Asia contains the two future economic giants, China and India
- The natural resource base of the planet will not support this without a change
- The old growth model will not scale
- Lifestyles and new growth patterns

The Annual MBA Roundtable presented us with world class speakers with very recent real world learnings, with a range from small to global issues, ideas and challenges. The focus on sustainability and the big picture is often lacking in the day to day learning rush.

An MBA participant
