Chapter 7

THE SLOW CONVERGENCE TRAP AND BAMT COUNTRIES

Reşat Can AKKAY[1]

1. INTRODUCTION

The trade globalization of the 1980s and the capital account globalization of 1990s led to a drastic change in the world economy. The increase in the volume of trade and financial flows triggered temporary high growth rates in most of the developing countries, especially in the emerging ones. On the other hand, most developing countries faced with the financial crisis, exchange rate crashes huge debt problems and income inequalities in the same period. The era after 2000 is called by some economists as the "Bretton Woods II" system due to the dominance of the US in the "vehicle currency business" as the main supplier of the US dollars and complicated financial products.[2] 2008 subprime mortgage crisis which existed basically due to the eagerness of the "financial ponzi scheme" has been the worst economic turmoil after the Great Depression, which affected the world economy via financial and trade contagion channels. In the beginning, the most affected countries have been advanced countries with highly developed financial markets. Later on, the economic problems in the advanced world led to an economic slowdown in the emerging market countries. Nowadays, some developed countries indicate signs for slow recovery while emerging market countries face economic slowdowns, high unemployment rates and output gaps due to the lack of foreign and domestic demand. In fact the economic performance of both country groups feels like that world economy might not return to its good days soon. Besides the changing structure of the production processes like Industry 4.0, the aging populations in both advanced and developing countries, the unfair income distribution, the conflicts between the benefiters and non-benefiters of the globalization are other issues in front of the countries.

Middle income trap is a relatively new and popular concept which seems suitable to discuss the above-mentioned problems from the developing countries' per-

1 Asst. Prof. Dr., İstanbul University Department of Economics, canakkay@istanbul.edu.tr

2 The "vehicle currency" is defined as the money that is accepted by every country as the medium of exchange and store of value at the international level.

empirical results are very sensitive to the time period and the data source which weakens the soundness of the results. For instance we conclude that Argentina will not be able to catch-up high income countries if we use the data for the 1969-2018 period but if make the same analysis for the 2000-2018 period there exist a probability to catch-up.

iv. BAMT countries seem to be in the trap according to the classical MIT definitions. According to the data Turkey is the country with the highest probability to get rid of the trap while Argentina is the country with the lowest probability. However we suggest that crossing an income threshold should not be interpreted as escape from the MIT.

v. We are not sure about the benefits of the categorization of the countries as "trapped" or "not trapped". As we mentioned before the results are very data and time sensitive. We find "MIT" a useful concept to discuss the developmental issues on the one hand. On the other hand the aggregation bias of the concept categorizes the country as a whole. Especially in the emerging market countries, different regions in the same country have been developing differently. One province could reach high income level while the other one struggles with poverty trap. Hence the aggregation bias of the MIT concept lowers the effectiveness of the recommended policies towards the solution of the trap.

vi. The difference between high income and upper middle income country is not only about the income levels. There are also differences about their social life, education, health, culture, happiness, etc. Hence we suppose that MIT is a useful concept to discuss the developmental issues but some dimensions of this concept is missing. According to our approach the "trap" problem should be discussed with the help of a composite index that covers all these dimensions.

vii. We prefer to use "slow convergence trap" instead of "middle income trap" because most of the emerging market countries seem to catch-up high income level countries sooner or later. The problem is about the time that they should spend for it. According to our investigation BAMT countries are all in the "slow convergence trap".

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