Inertia and Growth

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Concern is in vogue with regard to China's growth rate and its potential implications for the world. However, the same phenomenon can be observed in the U.S., Europe and other nations, including of course Mexico: the pace of economic growth has been descending. The question is why.

The simplest explanation for the tendency toward a lower growth rate is that as societies become wealthier, their incentives and needs that must be satisfied, change. The argument sounds reasonable: it is obvious that what an Indian who lives on less than a dollar a day requires is very distinct from the demands of a Swiss citizen, rendering it natural that India's growth rate would be superior.

In his famous book *The Cultural Contradictions of Capitalism*, Daniel Bell affirmed that growth laid the base for its own destruction because it generated people with little hunger for greater growth. In recent years, Edmund Phelps published a book* that follows that argument but leading to a very different conclusion: it is not that people stop having aspirations and needs, but that the environment has changed, making growth increasingly difficult. That is, it is not that capitalism engenders antibodies against growth but that the society tends to develop a form of new corporatism that impedes change.

Phelps' argument reminded me of what Galbraith said on the subject of the "military-industrial complex": it tends to paralyze development because it entails arrangements among enterprises and the government that make it difficult to change the status quo, the latter a condition necessary for the growth of the economy. Phelps denominates "corporatist complex" this type of corporatism, in which he includes the government, the legislature, the banks, companies and unions. For Phelps, there an implicit alliance among all of these interests to conspire against competition and innovation.

According to Phelps, there are phenomena known to all that stand in the way of growth and that have a bearing on the companies' incentives, the conditions for competition, the way in which the granting of bank credit has changed and the search for wealth ad hominem. However, what appears crucial to Phelps, and what is his true contribution to the discussion on growth, is that economic policy (in the broad, not the budgetary sense) is an institution in itself that reflects the values of the society and those very values bestow privilege on the preservation of what is. In a word, people do not want to take risks and that translates into social mechanisms that cause change and innovation to be impossible.

Those values procreate subsidy and protection mechanisms for enterprises and persons that have the effect of hindering the rise of new companies and development projects. In this manner, the laws, the regulations, the taxes, and the pension plans end up protecting what exists, making it unattractive for there to arise entrepreneurial spirits like those that forged wealth in former generations.

Phelps analyzes matters such as the following: bank credit was easier to procure decades ago than it is now, the creativity that is inherent in humans and that translates into the ability to identify new markets, solve problems and explore, does not prosper in an ambience of rigid rules, regulatory requirements and insurmountable fiscal issues; the enterprises that already exist and that have deciphered those pitfalls (typically a long time ago) entertain an incomparable advantage with respect to the individual attempting to create a novel venture. This adds up to people ceasing to be creative and to their adapting to the jobs or opportunities already in place instead of undertaking new ones.

If one were to go back in time to the histories of the growth of the world economies in the XIX century and the beginning of the XX, an era in which there were a lot fewer rules and regulations for everything, it is clear that innovators would run immense risks. An uncluttered comparison between the transportation systems of then and now sheds light on the different conceptions of what is safe: carts pulled by horses vis-à-vis automobiles equipped with every kind of protection. Phelps’ proposal does not involve returning to that time, but rather to focus attention on the costs implied in that entire world of protections and subsidies that has been constructed and that is, from his perspective, the explanation for the sinking growth rate.

If one extrapolates Phelps' analysis to Mexico, it would seem obvious that the strange collection of tariffs and subsidies that persist in a broad swath of the industrial sector is a factor that hinders innovation and, thus, growth. However, it is possible that the main explanation for the country's poor economic performance dwells elsewhere: nobody wants to assume risks because of the low probability of success, a circumstance that become more acute when there is so much uncertainty: part of which is caused by factors of the moment, like the recent American election, but above all by the physical and patrimonial insecurity that characterizes the environment. The pathetic performance of our economy is not the product of chance.

*Mass Flourishing

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