Endogenizing non-price competitiveness in a BoPC growth model with capital accumulation

Abstract

On a theoretical level this article revisits Thirlwall’s rule (or law) proposing a new channel through which it is possible to endogenize non-price competitiveness in the BoPC framework. We develop a model that formalizes the inverted-U relationship hypothesis that non-price competitiveness rises as countries move from a primary productive structure to light manufacturers and then decreases as richer countries get locked into antiquated industrial structures. We name it the stratiﬁcation mechanism. Finally we incorporate the supply side of the economy into the structure of the model in order to avoid the so called inconsistency problem.

Keywords: growth, Balance-of-Payments Constraint, Thirlwall’s law.

JEL: O10, O11, O40

1 Introduction

Post Keynesian models have emphasized over the years the importance of demand constraints on growth. One of the most successful empirical regularities among them is Thirlwall’s rule (or law). Given that countries cannot systematically ﬁnance increasing balance-of-payments imbalances, it proposes that there is an adjustment mechanism in aggregate demand that constrains growth. Therefore, in the long-run, growth is Balance-of-Payments Constraint (BoPC).

Despite its simplicity and powerfulness in explaining the great income divergence between advanced and developing/poor economies, there are at least two main issues still to be solved. The ﬁrst of them consists in the fact that foreign trade income elasticities - which represent non-price competitiveness of a country (or region) - are taken as exogenous. The second one is the inconsistency (or overdetermination) problem that may arise if the supply side of the economy is not properly incorporate into the model.

There have been a number of efforts trying to formally endogenize non-price competitiveness in the BoPC framework. In some cases there were also explicit concerns about the consistency of the model and the capital accumulation problem. However we are still building a consensus. Now it is well understood that distributive and technological questions matter and should be taken into account. But the subject is still open.

This paper aims to contribute to both issues by developing a model that formalizes the inverted-U relationship hypothesis that non-price competitiveness rises as countries move from a primary productive structure to light manufacturers and then decreases as richer countries get locked into old-fashioned industrial structures. We name it the stratiﬁcation mechanism. This mechanism operates in a such a way that opposite forces that acts over economic growth
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