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Aid and the Symbiosis of Global Redistribution and Development: Comparative Historical Lessons from Two Icons of Development Studies

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Table of Contents

Abstract

This study examines the question of aid effectiveness through a comparative historical analysis of the external financing constraints of two icons of development studies: South Korea and Brazil. The selection of these contrasting cases is based on a method of difference, designed to examine the predicaments of two countries attempting similar developmentalist strategies of sustained industrial policy through successive stages of industrialization, but with differences in amounts of aid supporting such strategies. This approach differs from the standard approach in the literature of examining economic performance among aid recipient countries and it is adopted as a means to highlight the challenges that some of the most successful and advanced late industrialisers of the post-war era have faced in the absence of aid. The comparison draws on an analytical framework that locates aid effectiveness in the interaction of both aid absorption (via current accounts deficits) and development strategy (via industrial policy), the latter based on the premise that unconstrained strategies of post-war late industrialisation have exhibited inherent structural tendencies to generate merchandise trade deficits. The interaction establishes an important, yet mostly overlooked, symbiosis between global redistribution and development.

This symbiosis is then demonstrated by the historical analysis of the external accounts of the two cases, which constitutes the original empirical contribution of the article given that inductive historical analysis of actual interactions between aid flows (or lack thereof) and external accounts has been essentially absent in the aid literature. Similarly, the literatures on industrial policy and developmental states tend to exhibit a domestic productionist bias that has also shunned serious analyses of the role of aid in supporting successful late industrialisation experiences. Accordingly, the case of South Korea clearly illustrates the crucial role that aid played in buttressing rapid late industrialisation against structural external constraints and financial vulnerabilities. The contrasting case of Brazil clearly demonstrates the constraints faced by late industrialising countries in the absence of generous supplies of aid and/or stable, secure and affordable finance. The conclusion reflects on some of the wider implications of these insights and also offers some comparative reflections on China as an alternative model for dealing with similar constraints.

Keywords

Aid (official development assistance); redistribution; political economy of development; industrialization and industrial policy; international finance and development finance; balance of payments; structuralist macroeconomics; South Korea; Brazil

List of Figures

Acronyms

BoK	Bank of Korea
BoP	Balance of Payment
DAC	Development Assistance Committee
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
IMF	International Monetary Fund
ISI	Import Substitution Industrialisation
ODA	Official Development Assistance
OECD	Organisation for Economic Cooperation and Development

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Aid and the Symbiosis of Global Redistribution and Development: Comparative Historical Lessons from Two Icons of Development Studies

In debates about the effectiveness of international development assistance (aid for short), only cursory attention has been given to specific historical cases about how aid actually has worked from a macro perspective. One reason for the lack of contextualised historical analysis has likely been the dominance of cross-country regression analysis in this literature, even despite the increasing criticism of this approach by leading figures in contemporary development economics, such as Deaton (2009).[1] Within such regressions, countries are treated as discrete observations, usually broken up by disassociated time intervals (or, in some cases, time series), in the search for generalizable albeit decontextualized patterns of aid absorption and/or impact on growth, consumption or investment across a large enough collection of observations to prove statistically significant and amenable to sophisticated econometric techniques. In the process, however, debates tend to increasingly revolve around methodological questions of econometric technique, as noted by Addison and Tarp (2015), without necessarily deepening our theoretical understanding of the complex causal processes that might be operating within individual cases. This literature thereby provides limited practical insight into why specific cases might or might not conform to the observed associations over time, particularly when the variables in question might be swinging about quite radically, as has been the case for most developing countries in the post-war era. Certain policy issues that are vital to understand the conditions that promote aid absorption, such as those concerning industrialization, are also generally abstracted if not ignored. As a result, conclusions about how aid might support economic development in specific cases tend to remain ambiguous and hypothetically drawn from theory (as is the case of the positivist deductive methodology used in econometrics), or even speculative and anecdotal. Rigorous systemic analyses of actual historical experiences over quite volatile periods of post-war history are neglected.

The notable outlier case that deserves attention in this regard is the Republic of Korea (South Korea), where aid was clearly involved in processes of rapid economic development from the early 1950s right up to the 1970s and, depending on how liberally aid is understood, even up to the 1980s. Aid to South Korea was not 'short, sharp and finite,' as suggested by Moyo (2009), although it was accompanied by an activist developmental state within a particular geopolitical setting, as has been widely discussed and debated in the literature on East Asian industrial policy. While its exceptionalism has often been asserted as a reason for the inapplicability of its lessons for other developing countries, the case nonetheless highlights certain fundamental

[1] The approach nonetheless continues to be defended in the aid effectiveness literature. For instance, in acknowledging the critiques and problems, Temple and Sijpe (2014) nonetheless argue that the approach is relevant for addressing questions that still need to be answered, although they are not clear what these questions are.

redistributive principles that are underemphasised within the productionist orientation of debates regarding East Asia. The exceptionalism of its geopolitical situation also highlights the fact that where there is political will, there is a way, in terms of how massive and sustained aid efforts can allow countries to overcome particularly vulnerable stages of development. Nonetheless, in the vigorous debates that followed the publication of the famed Asian Miracle report by the World Bank (1993), this particular perspective on the South Korean case has been generally neglected (albeit with some exceptions).[2]

An icon that serves as a poignant counter-example to South Korea is Brazil. Brazil might not seem to be the most intuitive choice given that aid was negligible in its post-war development, in contrast to countries that have received ample aid but with poor economic performance, as might be selected as cases to contrast with South Korea on the subject of aid.[3] Indeed, most cross-country studies of aid effectiveness generally adopt various measures of economic or more general development performance as their dependent variable. However, an inherent problem faced by such approaches is the question of whether poor performance is caused by the hypothesised failures of aid, or else more broadly by failures of economic development strategy, such as an absence of strong industrial policy, which the presence of aid might or might not influence.[4] In effect, robust industrial policy has been absent in the typical cases of failed aid usually selected from Africa and, hence, it is difficult to know whether the perceived failures of aid in these cases are instead reflections or symptoms of a broader developmental malaise over the last three or more decades.

The comparison adopted here avoids this problem by exploring the role of aid (or the absence of aid) in relieving (or not) particular external constraints faced by countries engaged in intensive strategies of late development. Brazil is a relevant comparator because it demonstrates the predicaments of a country attempting similar developmentalist strategies as South Korea (i.e. a serious, sustained and relatively successful practice of industrial policy through successive stages of industrialisation), but in the absence of ample amounts of aid or secure and affordable finance (besides in the 1970s, when Brazil had easy access to cheap debt financing and was able to

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[2] For one notable recent exception, see Yi Cocoman, Chung and Ree (2014).

[3] Although not specifically on the subject of aid, the comparison of South Korea and Zambia by Shafer (1990) is one example of this.

[4] Another problem with the econometric cross-country literature on these issues is the dilemma of how to deal with the relative weights and the causal significance of various variables within each case, rather than simply the weighting of cases. For instance, if aid effectiveness is treated along the lines of a multiplier effect, with or without time lags, then countries with strong performance and where aid is relatively insignificant (such as China or India) would have a strong effect on determining a positive association between aid and performance even though aid ostensibly had no causal effect on performance in these cases. Similarly, countries receiving relatively large amounts of aid but with poor performance due to factors unrelated to aid (such as Sub-Saharan African countries during the lost decades of the 1980s and 1990s) would have a strong effect on determining a negative association between aid and performance, even though, again, the association was ostensibly not due to aid but to much broader factors such as commodity crises, debt crisis, or structural adjustment programmes.

run large and sustained trade deficits for the only time in the post-war era). Hence, it is a useful counter-example to demonstrate the challenges that some of the most successful and advanced late industrialisers of the post-war period have faced in the absence of aid and/or preferential finance, and how they adapted to this particular constraint on their external accounts.

The choice of South Korea and Brazil is also pertinent precisely because comparisons of these two countries (and Taiwan) have been so iconic in the field of development studies more generally, even though these have mostly focused on industrial policy or developmental states,[5] and have excluded systemic analyses of aid. For instance, in the seminal work of Amsden (1989) on South Korea, she provides a rich discussion of the political economy of aid to the country (see chapter 2), although this is focused on the 1950s rather than subsequent decades and is substantiated by only a few cursory statistics on the volume of aid and its relative weight in the economy (e.g. see p.39). While she briefly mentions the role of aid in the 1960s (p.64) and does offer a more rigorous and systemic analysis of the role of external indebtedness in the 1960s and 1970s, and of successive stabilisation plans in the 1970s, her overall depreciative view on the role of aid is one that is characteristic of this literature, which tends to attribute primacy to the domestic and productive sources of successful economic transformation. From this perspective, detailed comparative analysis of the external accounts of both South Korea and Brazil potentially provides an important revision of the way that these two cases have been employed to build the contemporary theoretical corpus of development studies. Both provide strong (albeit contrasting) evidence to support certain classical propositions about the relationship between financial imbalances and late development, and the role that aid can play in bridging the two.

The methodology adopted in this article draws from comparative historical analysis, such as in the classic studies by Moore (1966) or Skocpol (1979). As explained by Skocpol (1979), 'the overriding intent is to develop, test, and refine causal, explanatory hypotheses about events or structures integral to macro-units such as nation-states…' particularly with respect to 'macro-historical phenomena of which there are inherently only a few cases [and too many variables]' (p.36). Here, the focus is more specifically on systemic trends and interactions of aid and other monetary flows on the external accounts of the two cases during the post-war period, informed by a general reading of their development experiences, as a logical starting point for contextualising and understanding aid effectiveness. This specific approach is also informed in theory and method by structuralist macroeconomics (e.g. Ocampo, Rada and Taylor 2009; Damill, Rapetti, and Rozenwurcel 2016), historical structuralism (e.g. Cardoso 2009), and more broadly by early development economics.[6] The emphasis on structural historical analysis helps

[5] For instance, see Gereffi and Wyman (1990), Evans (1995), Kay (2002), Kohli (2004), and Schrank (2007). McGuire (2001) also offers an interesting comparison of East Asia and Latin America from the perspective of social policy.
[6] These more inductive approaches are different from – but could be compared to – the analytical narrative approach of Bates, Greif, Levi and Rosenthal (1998) and Rodrik (2003), which instead draws from a rational choice and game theoretic approach to institutionalism and political economy.

to highlight the constraints within which institutions operate and actors make choices and strategize under the influence of a range of incentives and compulsions, and thereby opens up space in economic analysis to inform (and be informed by) broader political economy questions. Indeed, it offers one effective approach to the 'importance of disaggregation, and the need to account for country-specific situations and problems,' as identified by Addison and Tarp (2015, p.1), albeit while still considering common systemic features faced by developing countries in the global economy. Notably, this reference to structural constraints is not used to imply determinism, as is often criticized by post-structuralist authors, nor is it used to emphasize institutional stability and continuity, as criticised by Streeck and Thelen (2005, p.6) with respect to contemporary institutionalist analysis. Rather, it is understood here, as in early development economics, as a crucial dimension that potentially destabilizes developing economies, thereby acting as an important determinant of institutional change, the analysis of which needs to feature centrally in political economy studies of development.

The analytical framework of this comparative study starts from the premise that aid, understood in a macroeconomic sense as a monetary flow within the balance of payments, is absorbed and has effects through trade deficits, and in interaction with other flows on the external accounts. This association of absorption (of aid or net external finance more generally) with trade deficits highlights an important symbiosis between international redistribution and national development given that late development (understood as centrally involving late industrialisation) has strong tendencies to generate trade deficits (both merchandise/goods and services). Given this tendency, it thereby requires net inflows of foreign resources. From this perspective, aid effectiveness needs to be assessed relative to both the redistributive and the productive wings of the developmental bird, so to speak, that is, the interaction overtime between external accounts and economic development strategies aimed at industrialisation within particular cases. As noted by Fischer (2009), this implication was clearly understood in early development economics and served as the foundational post-war rational for aid, although it has been essentially absent from the contemporary aid literature. The monetary side of aid absorption is recognised by some specialised tangents of this literature, although it is rarely if ever associated with productive questions of industrialization within these tangents. Otherwise, the more general literature on aid effectiveness generally remains insulated from even these specialised monetary insights.

The symbiosis between redistribution (aid) and developmentalism (industrialisation) is nonetheless strongly evidenced by the iconic country cases that have shaped theory and debate in development studies. In particular, the case of South Korea clearly illustrates the crucial role that aid and other implicit forms of support, including generous supplies of official finance, played in buttressing rapid late industrialisation against structural external constraints and financial vulnerabilities, thereby playing a key role in its rapid emergence as an industrial power well into the 1970s and arguably even into the 1980s. In particular, aid and debt allowed the country to run deep merchandise trade deficits throughout this entire period, to an extent never observed in Latin America, ironically despite the reputation of the country as an export-oriented poster child. In this sense, the country had not solved the predicament faced by Latin Americans of an increasing import intensity associated with late industrialisation (whether ISI or export-oriented), particularly with shifts towards more capital-intensive industries. Rather, its ability to increase exports was arguably permitted by its capacity to increase imports, which was crucially funded by aid and other forms of support. The fact that aid was associated with such deficits also meant that aid absorption was not particularly problematic in a macroeconomic sense, although this was predicated on strong state-led industrialisation policies. As an important corollary, aid and debt also permitted South Korea's emergence to occur without reliance on FDI and, hence, through mostly national forms of ownership. In sum, aid provided development space, although a systemic evaluation of aid effectiveness also needs to consider the policies that actually took advantage of this space to produce development (i.e. industrialisation).

The contrasting case of Brazil clearly demonstrates the constraints faced by late industrialising countries in the absence of generous supplies of aid and/or stable, secure and affordable finance. Indeed, aid was only significant in Brazil for a short spell in the 1960s, although this occurred in the context of merchandise trade surpluses and was thereby rendered redundant in a macroeconomic sense, except by way of its contribution to the counterbalancing the chronic service and income deficits, but not in terms of enhancing the capacity to run development-induced merchandise trade deficits. Moreover, in the absence of generous external funding conditions, Brazil's development strategies quickly become constrained, as expressed by recurring balance of payments crises and a regular reliance on FDI. From this external perspective, the current accounts of Brazil reveal a remarkable lack of transformation away from a pattern of external integration inherited from the early post-war period, despite quite deep structural transformations in the domestic economy. These predicaments are most quintessentially expressed in terms of merchandise trade surpluses financing service and income account deficits, with the net current account balance often in deficit and financed through expensive, volatile and regularly punitive private financial flows.

This analysis is made in two sections. The first section lays out the foundational understanding regarding the symbiosis between aid absorption and trade deficits on one hand, and the relation between late industrialisation and trade deficits on the other hand. The second presents the comparative empirical analysis of the two cases. The conclusion then reflects on some of the broader lessons that can be distilled from these two cases on the structural difficulties with sustaining significant degrees of publically funded international redistribution within the contemporary context of global financial imbalances. It also offers some reflections on the case of China, as an alternative to the Brazilian model of dealing with external financing constraints in the absence of aid or other preferential financial flows.

1 Redistribution and Development from a Balance of Payments Perspective

Aid absorption needs to be understood (and was understood by early aid advocates) as a function of allowing countries to fund development by running trade deficits and, by consequence, net monetary inflows. As discussed in Fischer (2009), this understanding was a key point of departure for many of the pioneers of development economics in the 1940s and 1950s, who generally conceived of the role of aid within a much broader perspective of late development and balance of payments disequilibria. There are two symbiotic aspects to this understanding: the fact that aid absorption, in a macroeconomic sense, occurs through trade deficits, and that unconstrained late industrialisation has a strong propensity to generate trade deficits.

1.1 Aid absorption and trade deficits

The first aspect is not a theoretical proposition as such, but is simply a logical deduction from the balance of payments accounting identity, as is recognised in the specialised literature on the macroeconomics of aid (e.g. see Rajan and Subramanian, 2005; Hussain, Berg and Aiyar 2009; Martins 2011; Temple and Sijpe 2014). By definition, the sum of all components in the balance of payments must equal zero, i.e. all income and asset transactions must be accounted for in the identity. The current account includes the trade balance (exports minus imports of goods/merchandise and services), the income account (which is generally dominated by profit remittances and interest payments on debt, as well as payment of wages to non-residents), and current transfers (which include official transfers, i.e. aid, as well as workers remittances, etc.). The capital/financial account includes net changes in debt, net direct investment, net portfolio investment (e.g. stocks and bonds), net 'other' investment (e.g. currency transactions and bank deposits, derivatives, etc.),[7] and net changes in reserves (technically part of the financial account although often reported as a separate account). Errors and omissions reflect the net discrepancy, i.e. the residual that is left over when the sum of discrepancies occurring on any of the accounts does not equal zero.[8] They can

[7] The IMF only started to recommend reporting derivatives as financial assets, rather than on the income account, in a supplement to the fifth edition of the Balance of Payments and International Investment Position Manual (BPM5) in 2000. Derivatives have been reported under a separate accounting category since the sixth edition of the Manual (BPM6), published in December 2009.

[8] The current accounts of the major OECD countries started to develop noticeable and increasing discrepancies as early as mid-1970s, and then the financial accounts and net errors and omissions in the world balance of payments also started to develop increasingly abnormal discrepancies in the 1980s. The IMF formed a working group to investigate these discrepancies in 1983, which concluded by the early 1990s that the world capital account statistical systems were in a state of crisis (IMF 1992). This work remains active under the IMF Committee on Balance of Payments Statistics (e.g. see IMF 2015). Kregel (2008: 25-8) also reminds us that these accounting methods are out of date with respect to changes in the global organisation of production and trade, insofar as their design is based on an antiquated conception of the post-war Bretton Woods world, in which national economies traded final goods and services with each other, and private capital flows were limited. 'Paradoxically,' he argues, 'in the modern world, capital flows may no longer represent transfer of resources or the financing of

give indications of illicit flows such as capital flight or tax evasion, although not entirely given that many illicit flows cancel each other out and hence do not show up as net errors and omissions.[9] Many discrepancies are also not due to illicit flows.

In somewhat disaggregated form, the identity can be represented by the following equation:

(X-M) + net income + net transfers + net Δ debt + net FDI + net other I + Δ reserves + E&O = 0

The well-known implication is that the current account effectively equals the inverse of the capital/financial account or, even more narrowly, the trade account equals the inverse of everything else:

(X-M) = – (net income + net transfers + capital/financial account + Δ reserves + E&O)

For the purpose of this analysis, we can simply focus on this external account identity, abstracting from its interaction with domestic dynamics (as aid absorption is often discussed).[10] Excess consumption on the trade account (of goods or services) must be externally funded through one of the other accounts (income, transfers, financial or reserves), as a means of providing the excess foreign exchange needed in order to pay for the shortfall that is not earned through exports.[11] This constraint is not necessarily binding for countries that possess reserve currencies (principally the US) given that they can finance trade deficits with domestic money supply. However, countries without this privilege of global seigniorage rights face hard constraints and must finance the excess of imports over exports through an inflow of foreign exchange on one of the other accounts (including through the use of reserves, as a stock of previously saved foreign currency). Inversely, if the excess foreign exchange that is earned through a trade surplus is not used for some other foreign currency expenditure or transfer on one of the other accounts, then at the very least it is held in cash or reserves, which is technically counted as an outflow in the sense that it does not enter the domestic economy, even though it adds to the stock of foreign assets held by the country. In this manner, net

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productive activity, and goods flows may no longer represent production of final goods for import or export.'

[9] Indeed, as noted by Naylor (2004[1987]), a problem with much of the literature on illegal finance is that it only considers the evasion side of illegality, whereas much of illegal activity involves laundering, in which the intention is to make illicit flows appear licit.

[10] Aid absorption is usually expressed by way of the interaction of external accounting with national accounting identities, whereby a trade deficit represents that a country is consuming more than it is producing and the excess consumption can, in principle, be attributed to private or public/government consumption, or investment in the domestic economy. For instance, see this approach in Temple and Sijpe (2014), who test for the association between aid and these various components, or else Hussain et al (2009) or Martins (2011) regarding the relation of aid to both current account and fiscal deficits. Both Morrissey (2015) and Mosley (2015) are similarly interested in the interactions between aid flows and domestic fiscal behaviour.

[11] This description is obviously and necessarily simplified and artificial; in reality, net balances only become apparent after the fact.

inflows of foreign exchange are absorbed into domestic economies through the consumption of imports, not through the exchange of currencies, which simply shuffles ownership of foreign and domestic assets (i.e. currency).

This logic derived from the external accounting identity does not imply a direction of causality between trade deficits and the financing of trade deficits, unlike theoretical economic models that impose assumptions about causality. In other words, the appearance of a trade deficit on a country's external account could be interpreted from a 'real' supply side perspective, whereby the other accounts passively adapt and supply the finance needed for a trade deficit, or else it could be interpreted from a monetary demand-side perspective, whereby the supply of finance determines the ability of a country to demand and consume net imports and run a trade deficit. In either case, a constrained supply of finance constrains the ability of countries to run trade deficits and, hence, the appearance (or lack) of trade deficits can offer some insights into the external financing conditions faced by that country.

Aid is recorded as a positive inflow on the current transfer account of the recipient country and, in this sense, is absorbed via trade deficits (i.e., aid that is actually transferred to a country, versus the monetary circuit of technical assistance, which mostly remains in the donor country). Its contribution as a monetary flow must therefore be seen relative to the other flows on the external account given that it is one among many means of funding trade deficits. Indeed, a weakness in some of the macroeconomic literature on aid is that these counterbalancing dynamics are not fully considered, perhaps due to the use of *ceteris paribus* logics to analyze the impacts of increased aid flows. For instance, while the balance of payments relation is recognized in the literature on the potential 'Dutch disease' effects of aid, that is, the effect of increased aid flows on exchange rate overvaluation (c.f. Rajan and Subramanian, 2005; Elbadawi, Kaltani and Soto, 2012; Berg, Portillo and Zanna 2015), the Dutch disease argument is only relevant insofar as it assumes that increased aid is not compensated by increased trade deficits as the principle mechanism of aid absorption, because otherwise there would be no danger of overvaluation (see this argument in Fischer 2009).

Alternatively, aid could equally serve to fund deficits on any of the other accounts, such as profit remittances, interest repayments on debt, various net outflows on the financial account, or else reserve accumulation. Serieux (2011) characterizes these as 'reverse flows'. Hussain et al (2009), Martins (2011) and Berg et al (2015) are also implicitly motivated by this possibility in their attempts to measure the degree to which aid flows are absorbed via current account deficits and/or spent through fiscal deficits, versus being accumulated as reserves and/or sterilised by central banks. Again, the position of the trade account in these considerations is important given that 'reverse flows' would invariably occur in the context of a trade surplus, in which aid would accentuate a situation in which foreign exchange is already in surplus on the trade account and is thus flowing out through one of the other accounts (or being accumulated as reserves). While trade deficits allow for the net transfer and absorption of aid (or other financial resources) into a country, trade surpluses effectively eliminate this possibility for aid to provide a net monetary contribution to the domestic economy. In the latter case, aid still might (or might not) provide some non-monetary benefits such as skills transfer or technical assistance, but it does not serve its primary redistributive function of providing net monetary resources to the recipient country (unless saved as reserves, in which case, it could be absorbed or used at some point in the future).

From this broader macroeconomic perspective, it is also notable that projections of aid irrelevance tend to circulate in times of financial profligacy, such as during the 1970s or before and after the 2007-09 global financial crisis.[12] During these phases of global financial expansion, alternative supplies of private finance were abundant and at their historically cheapest levels, hence displacing the need for aid to finance trade deficits. Nonetheless, it is during times of crisis, when these private supplies of finance to peripheral countries tend to dry up, that the aid industry reasserts its very pivotal and powerful leverage, particularly gatekeepers such as the World Bank and the IMF, given that strategic injections of aid can help to stave off balance of payments crises, whether these are driven by trade or other deficits on any of the external accounts.

1.2 Late development and external imbalances

The second complementary aspect concerns the external imbalances inherent to late development, that is, the inherent tendency for unconstrained late industrialization to generate trade deficits, especially in the post-war era. As discussed in Fischer (2009), the reasons are structural, in that late development is typically very import-intensive, and structural/technological dependence results in a strong inelasticity of imports to growth, in particular with respect to capital or technology-intensive and intermediate imports. Development is therefore constrained by the supply of foreign exchange to fund trade deficits, in addition to the broader political economy constraints and challenges involved in processes of late industrialisation, as amply discussed, for instance, in the contemporary literature on industrial policy or developmental states. The foreign exchange constraint (or gap, as it was often called) thereby generates a need for affordable, stable and secure supplies of foreign currency in order to avoid impeding or stunting industrial development through this particular channel. The strategic role of aid is based on overcoming these foreign exchange constraints. It is not based on financing overall investment or government spending, which can be financed domestically and hence does not necessarily require the injection of foreign currency.

This understanding is evidently based on the assumption that industrialisation is a necessary (although not necessarily sufficient) condition for development, as was almost universally regarded by the pioneers of development economics, many of whom called themselves ‘structuralists’ given their emphasis of structural impediments to growth that tended to emerge through the course of industrialisation.[13] For instance, Prebisch (UN 1950)

[12] For instance, Addison and Tarp (2015) refer to this argument in their introduction.
[13] Prominent pioneering structuralists include Paul Rosenstein-Rodan, Ragnar Nurkse, Gunnar Myrdal, Alfred Hirschman, Paul Singer and Raul Prebisch. Arthur Lewis apparently avoided

argued that industrialization in export dependent economies would manifest tendencies of external disequilibria in the form of 'trade gaps,' alongside internal disequilibria in the form of inflation and repressed production and consumption due to constrained import volumes or supply rigidities in domestic food production.[14] Hirschman (1958) similarly associated himself with structuralism by identifying the domestic food producing and the foreign exchange earning sectors as structural bottlenecks to industrialisation. Lewis (1978) argued that parallel transitions such as urbanization and urban growth would also exacerbate the demand for capital and technology intensive imports, at least when they occur through the extension of modern urban infrastructure rather than slums.[15] Furtado (1973) contended that these impediments (or constraints) arise even in the absence of the industrialisation of production, through the industrialisation of consumption in otherwise non-industrialised economies.[16]

The structuralist position generally differed from modernisation theorists in that impediments were seen as structurally inherent aspects of late development already unleashed, based on the technological and input characteristics of production and consumption, rather than characteristics of some pre-transitional, socio-cultural, or institutional setting. Impediments would also tend to intensify the more a country is a late-comer given increasing lags from the technological frontier, or else the more a country is late in the demographic transition given that this generally results in more rapid population growth and subsequent urban growth. The inelasticity of the import demands in particular meant that external constraints could not be overcome through either market clearing prices or through macroeconomic demand management, both of which might even exacerbate the problem. The more critical of the pioneers further emphasised that the peripheral and subordinate integration of most poor countries into the post-war world economy, in particular through the increasing dominance of northern transnational corporations, accentuated these constraints by exacerbating technological dependence as well as terms of trade declines or outflows of wealth at the expense of import capacity.

Indeed, the earliest theorisations of dependency in the 1950s by Celso Furtado and Osvaldo Sunkel – both colleagues of Prebisch – were based on extending this structuralist understanding in the context of contemporaneous balance of payments crises in Brazil and other Latin American countries, which were occurring following a decade of post-war growth and industrialisation in the absence of generous supplies of foreign finance (as discussed in the next section). Despite the caricature of these authors as ardent advocates of import

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the 'structuralist' appellation although, like many structuralists, his modelling was classically inspired.

[14] See Polanyi-Levitt (2005) for a good summary of this position.

[15] Lewis (1978) proposed that rapid urban growth above a certain rate would tend to induce trade deficits, even in the earlier cases of European or North American urban growth, and thereby determining whether a country would be a capital importer or exporter.

[16] Indeed, a fallacy within much of the post development literature is the advocacy of alternatives to industrial capitalist development within economies that are nonetheless increasingly integrated into what Furtado (1983) called 'industrial civilisation' via consumption, even if not through production.

substitution industrialisation (ISI), they already recognised in the 1950s – well before the critiques of Bhagwati and Krueger (1973) and their colleagues – that ISI strategies did not effectively curtail the external constraints. Instead, ISI tended to exacerbate the constraints given the import intensity typical of most import substitution industries, particularly in the shift to heavier more capital-intensive industries (e.g. see Furtado 1956 and 1973). In the then-famed debates between 'structuralists' and 'monetarists' in Latin America in the late 1950s (see Seers 1983), the former highlighted that these crises could not be solved by austerity and structural adjustment given their inherently structural character, which would tend to reassert itself once growth would recover from austerity.

As these critiques were radicalising in the South, the structuralist view was also mainstreamed, and it became as much a Washington as a Southern consensus, even though the former came to be displaced by the new so-called Washington Consensus of the 1980s. The classic two-gap model of Chenery and Strout (1966) emerged as the formal representation of this mainstream consensus.[17] Their model was structuralist in that they recognized limits to the capacity of industrializing countries to expand export earnings rapidly enough to earn the foreign exchange required for complementary imports of capital and intermediate goods, which thereby provided theoretical justification for aid. Indeed, the now-standard epochal appellation of this earlier era as 'structuralist' is best understood as referring to this more mainstream structuralism of US economists such as Chenery, under whose leadership the World Bank actually endorsed economic planning and against whom the 'counter-revolution' was waged within the Bank itself in the early 1980s.[18]

The ideal of how aid could assist in overcoming these external constraints was notably informed by inter- and postwar experience in Europe. Balance of payments crises in Europe in the 1920s and 1930s, particularly in central and eastern Europe, highlighted the disequilibria typically faced by peripheral late industrialisers,[19] while the post-war Marshall Plan in turn came to epitomise how aid could prevent such crises, particularly given that it was instituted in 1947 following severe balance of payments problems in Europe and the risk that Europe would fall anew in financial crisis. While the Marshall Plan was about reconstruction rather than development *per se*, its strategic role was similarly found in the fact that reconstruction was hugely import-intensive, in large part because industry had been crippled in Europe by the war, leaving the US as the only industrial economy capable of filling the large-scale demand for the capital-intensive inputs required for reconstruction. As a result, reconstruction was balance of payments constrained, as distinct from domestic savings constraints, and it quickly generated large trade deficits with the US, which the Marshall Plan was designed to finance. While revisionist assessments

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[17] See Morrissey (2001: 39-40) for a brief discussion of the Chenery and Strout model and a limited selection of subsequent authors extending the 'gap models'. Note that this family of gap models, which distinguish between foreign exchange gaps and savings gaps, should be differentiated from the savings-gap model promulgated by Sachs et al (2004) which, as pointed out by UNCTAD (2008: 56), borders on tautology.

[18] See Toye (1987), who popularized this appellation of counterrevolution.

[19] See Polanyi-Levitt (2006) for a discussion of the analyses of this period by both Keynes and Polanyi.

of the Plan have tempered perceptions of its relative importance in the reconstruction in Europe (e.g. see DeJong and Eichengreen 2003; Eichengreen 2010), its contribution of around two percent of GDP of both the USA and the receiving European countries was nonetheless important in relaxing the foreign exchange constraints of reconstruction. The Plan needs to be evaluated in this strategic marginal sense, not in terms of its overall contribution to investment in Europe at the time, which was predominantly European. Moreover, while it has often been criticised as merely guaranteeing both the purchase of US exports as well as the repayment of US loans, it was precisely in this financial dynamic that its redistributive function was based.

Another influence, emphasised by the more radical literature, was based on historical analyses of earlier European industrialization and state formation, which also manifested tendencies for running trade deficits. The European powers that possessed significant colonies used these colonies to manage their international payments imbalances (those powers without colonies were in much more dire straits in this regard, which perhaps helps to explain the impulse behind the rush to amass colonies in the late nineteenth century, even if those colonies did not turn out to be particularly profitable). Many scholars dispute the claim that colonialism financed the industrial revolution in Europe due to evidence that industrialization was funded mostly from domestic European sources. For instance, Milanovic (2003: 672) adopts this position with reference to Bairoch (1997). However, it is quite plausible that colonial surpluses, especially with India in the case of the UK, played a crucial strategic marginal role in allowing the colonial powers to manage their balance of payments vulnerabilities in the context of industrialization, nation state building, and war craft, particularly with respect to other contending industrial powers. Referring to some of this earlier literature, Arrighi (2008: 137) notes that Britain used its trade surplus with India, at least from the mid-nineteenth century onwards,[20] and India's surplus with all other countries, to balance its trade deficit with the rest of the world. He also suggests out that Britain's adherence to the gold standard in the nineteenth century and its consolidation of global financial and commercial supremacy were closely connected to its extraction of tribute from the Indian subcontinent (the Home Charges) combined with the Bank of England's control over India's foreign exchange reserves.[21] Under the exceptional circumstances of the US, industrialisation was fuelled by a continuously expanding and very fertile agricultural frontier swept clear of its original inhabitants through genocide, which was then filled by unprecedented levels of immigration from Europe (a form of human trade

[20] As classically documented by Mukherjee (1974), Britain's trade balance with India went through a dramatic reversal between 1810 and 1830. Specifically, it had a large trade deficit in textiles with India in the early nineteenth century, as a mercantile expression of its import and re-export of Indian textiles. However, by the 1830s, Britain was earning a large trade surplus in textiles with India, as high tariffs were imposed on the import of Indian textiles to Britain at early as 1813, while textile manufacturing was repressed in India and to a large extent substituted by the rise of English textile manufacturing, based on the import of raw cotton from India. These were the objective conditions – later continued under direct rule – that gave rise to the Swadeshi movement under Gandhi.

[21] See a similar discussion in Desai (2013). See Gordon (2010) for an estimate of the Dutch colonial surpluses from Indonesia from 1878-1939.

deficit never to be rebalanced with Europe), travelling on infrastructure that had been heavily financed by bond holders in London.[22] Hence, as conceived in this manner, many of the early structuralists conceived of aid in the context of de-colonisation in the 1940s and 1950s as a matter not of altruism but of reparations.

Under this ominous pre and post-war shadow, and regardless of the differences on specific points or theoretical approaches, a strong consensus was thus formed in early development economics that contemporary countries attempting late industrialisation would have a chronic tendency to run trade deficits. In a world with limited private financial flows (besides foreign direct investment), as was the case in the 1940s and 1950s, these countries therefore tended to experience chronic balance of payments crises. Alternatively, if they ran trade surpluses, they often did so through import austerity, as was the case in the immediate aftermath of the Latin American debt crisis in the early 1980s.[23] The issue was not about export orientation versus import substitution, but about exports keeping up with the financial and capital requirements of industrialisation that, by the very fact of being late, implied import substitution through one means or another.[24] The choice was effectively between trade deficits balanced by some channel of monetary inflow, or else choking growth.

Indeed, as argued by some authors such as Amsden (1989; 2007), import substitution and export oriented industrialisation strategies were never really in antipathy, but instead played complementary roles in most successfully industrialising countries. This point is implicitly supported by Naughton (1996), who argued that Chinese industrialisation (at least up to that time) was also best characterised as a combination of import substitution and export orientation. Both strategies emerged as two post-war responses to foreign exchange constraints, in coordination with strategies on the financial account such as encouraging FDI or other inward financial flows, or accumulating debt, as means to finance trade deficits through the financial account. Most

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[22] See Lewis (1978) for details on immigration and finance. See Alessio and Renfro (2015) for a compelling rethinking of the United States' association with empire.

[23] As argued in the seminal post-mortem analysis of the debt crisis by Carlos Diaz Alejandro (1984), Latin American governments were able to generate substantial foreign exchange surpluses very quickly within a year of the 1982 crisis by simply sending their countries into crushing contractions. The immediate tool was stiff devaluations, which caused sharp reductions in imports while exports could barely respond due to lack of capacity or lack of external demand. Import reductions then crippled domestic manufacturing. In most cases this was combined with monetary restrictions, sharp reductions in public expenditures, and, in particular, 'the worst was the violent reduction in investment, which impaired not only present but future growth…' (p.363). He also pointed out that none of this solved the problem of high inflation, eroding 'the credibility of those who argue that elimination of inflation is indispensable for improving the balance of payments problem' (p. 365). Rather, the main goal achieved through such violent structural adjustment was that these economies were released from their foreign exchange constraint, thereby allowing the rapid repayment of foreign debt. Thus strong pro-cyclical economic policy applied in the midst of a sharp economic downturn temporarily fixed the external problem for long enough to remove international creditors from any major danger of default. We were then delivered a new monetarist consensus from Washington to clean up the resulting internal mess.

[24] Furtado (1973) clarified that import substitution was as much a de facto logical corollary of late industrialisation as it was a specific policy choice; also see Hirschman (1968) for a similar clarification of different types of ISI.

countries have followed a mix of both strategies and the structural constraints and opportunities to choose between different mixtures is arguably crucial to understand the political economy dynamics underlying post-war development in various countries and world regions. The option of using trade surpluses rather than deficits to drive late industrialisation, through augmented external demand rather than net financial inflows,[25] has been a relatively new phenomenon among developing countries and is part of the China puzzle to this question, although only after the late 1990s. Nevertheless, even in China, these external constraints are a hugely underrated and overlooked consideration in the political economy of the country's development in the reform period, as argued by Fischer (2010).

From this perspective, aid was clearly conceived in early development economics as constructive only insofar as it enables an industrialising country to run persistent trade deficits, albeit deficits that result from productive accumulation rather than from simply terms of trade or other contractionary shocks. This is quite different from the savings-gap model of Sachs et al (2004), who argue that the savings gap derives from poverty itself while ignoring industrialisation or the distinction between domestic and foreign savings. Rather, if aid was to have a constructive role, it was seen as a strategic injection to overcome particular financial vulnerabilities faced once development was already well underway.

This latter conception of the role of aid – as a strategic support for industrialisation – has been essentially absent in the extensive contemporary literature on aid. The more general relation between imbalances and late development has been discussed by some post-Keynesian economists, most notably Kregel (2008). Similarly, Thirlwall (1979; 2011) has continued to expound the idea of 'balance of payments constrained growth', while Bresser Periera (2011) or Cimoli and Porcile (2014) also explore Thirwall's approach with reference to the Latin American tradition of structuralist economics. However, again, these post-Keynesian authors do not specifically focus on aid and have made little if any inroad into the aid literature (with the exception of Fischer 2009), even though the principles they explore are fundamental to understanding the developmental potential of aid and the redistributive imperative of development more generally.

In the more mainstream literature, there are some brief acknowledgments and summaries of the earlier tradition of gap models, such as in Morrissey (2001: 39-40) or Addison, Mavrotas and McGillivray (2005), although these are rarely if ever extended or connected to discussions about late industrialisation.[26] As discussed above, the relation of aid absorption to trade deficits has been analyzed by a specialized tangent of macroeconomists, usually with some connection to the IMF. However, again, these analyses have been quite insulated from the broader aid literature and also avoid the central role of industrialization in creating the ideal conditions for aid absorption and effectiveness, perhaps in part because of taboos regarding industrial policy that

[25] See Kregel (2008) for a discussion of these two approaches.

[26] As noted previously, the so-called 'gap models' of Sachs et al (2004) do not distinguish between foreign and domestic savings and hence do not fall into this category.

have been dominant in these academic and policy communities, at least up until recently. For instance, it is notable that in the recent special issue of *World Development* on the macroeconomic management of aid edited by Addison and Tarp (2005), there is effectively no discussion of industrialization or industrial policy in any of the assembled articles. Rather, recognitions of gap models or questions of aid absorption are mostly used as entry points for cross-country regression analyses that abstract from questions of industrialization, or else that briefly alude to industrialization in a reductionist manner by using one or two variables that purportedly reflect economic structure.

As a result, the synergy of the redistributive dimension (i.e. the aid-deficit relation) and the developmental dimension (i.e. industrialization and imbalances) has been more or less absent in the broader aid literature. The oversight amounts to a proverbial elephant in the room in discussions of aid effectiveness, and is characteristic of both aid proponents and critics. Instead, the discussion of aid effectiveness has generally veered towards an institutional 'good governance' lens, focusing on quality of domestic institutional environments and related issues such as accountability, corruption, rent seeking, elite capture, and divergence of resources away from their intended purposes.[27] These latter contributions focus on what might be considered as the domestic sphere of governance in donor-recipient relations, and in particular on how aid distorts elite incentive structures, although they struggle to account for the fact that the starting point of successful developing countries exhibited many of the same characteristics of poor institutional quality and governance as the less successful cases, as repeatedly argued in the work of Khan (e.g. 1995; 2000; 2006). As a result, even though the question of aid effectiveness has received profuse attention, the broader context in which aid effectiveness was originally conceived, particularly with respect to industrialisation, has been mostly overlooked in the recent debates despite its arguably continual relevance.

2 Comparative Analysis of Two Balance of Payments Histories

Comparative historical analysis of a few iconic and crucial cases demonstrates the synergy of redistribution and development, and thereby helps to re-centre our attention on this dimension in the aid literature. As discussed in the introduction, the two cases chosen for this purpose are South Korea and Brazil based on their similarity of sustained and relatively successful practices of industrial policy throughout the post-war period, while differing in the presence or absence of ample amounts of aid or secure and affordable finance (besides in the 1970s, when Brazil had easy access to cheap debt financing and was able to run large and sustained trade deficits for the only time in the post-war era). The counter-example of Brazil in this sense helps to demonstrate the challenges that some of the most successful and advanced late industrialisers of the post-war period have faced in the absence of aid and/or preferential

[27] For good examples, see the work of Bräutigam (2000), Knack (2001), and Bräutigam and Knack (2004).

finance, and in particular how they adapted to this particular constraint on their external accounts.

For the sake of analysis, it is sufficient here to focus on the external accounts of these two cases, supplemented by a general reading of their post-war development experiences. The approach is inductive, involving a thick description of historical trends within the complex and interdependent structure of the balance of payments. This approach is original insofar as it has not been conducted in the aid or broader development studies literatures even though it provides important clarifications on the role of aid (or its absence) in these historical cases that have informed so much of the corpus of theory and policy in the field of international development. Indeed, as discussed in the introduction, detailed and systemic consideration of this dimension has also been largely absent from the parallel literature on industrial policy and developmental states. Comparison with Brazil in this sense serves as a useful corrective to this otherwise rich literature, by putting into sharp contrast the extent of the differences that these two iconic countries faced on their external accounts.

The data has been compiled from a variety of sources. More recent data have been taken from the online IMF balance of payments and international financial statistics databases, although these currently only provide data from 1976 onwards, whereas the key period of interest for both cases precedes this date. In case of South Korea, earlier data is derived from two sources: from Rhee (1973) for data from 1961 to 1972, supplemented by some historical data published by Bank of Korea (BoK 1995). The latter source starts from 1945, or from 1950 for more complete data, although a starting date of 1953 is chosen for this study given that this year marked the end of the Korean War. The BoK source is also very partial, hence data series for some accounts are not available prior to 1961 and there is a gap in the data between 1973 and 1975 because of the reliance on Rhee (1973) for more detailed data. The OECD DAC database is used for data on official development assistance, although these data only start in 1961 – they are compared with the current transfers data in the current account data as an alternative measure of aid flows. These would be ideally broken down by the various current transfers sub-accounts (i.e. general government, other sectors, workers' remittances, and other transfers), although, in the sources consulted, these decomposed data are only available from 1976 onwards in the IMF BoP data, by which point aid in the form of current transfers had become very marginal in the case of South Korea. Prior to 1961, data on grants provided by BoK (1995) are used. Given that most aid sent to South Korea in the 1950s was in the form of grants, this offers a good measure of total aid flows. The case of Brazil was facilitated by access to the database compiled by Giambiagi, Villela, Castro and Hermann (2011), which offers sufficiently detailed balance of payments and summarised national accounting and related data from 1945 to 2010.[28]

The various accounts on the balance of payments are presented as net balances rather than gross flows. There is a case to be made for looking at

[28] I am especially grateful to Lavinia Barros de Castro for giving me access to their excel spreadsheets, updated to the 2014 data, and permission to use the data for this research.

gross flows, particularly in periods when gross flows expand rapidly on the financial accounts, which would not necessarily appear in the net balances (e.g. this case is made by Akyuz 2015). However, this case is more pertinent for the latter half of the post-war period, from the late 1960s onwards, when private financial flows became increasingly liberalised and the volatility of gross flows became a major factor in global financial stability. Some discussion of gross merchandise trade flows is nonetheless made at the end of this section.

These balances on the disaggregated external accounts are also normalised as percentages of nominal GDP converted to US dollars at market exchange rates, given that the external account data is invariably in current US dollars. The use of market exchange rates for GDP conversion is the most appropriate manner to assess the weight or international purchasing power of the local economy relative to external transactions made mostly in US dollars; purchasing power parity measures of GDP would not be appropriate in this sense.[29] However, as a result, the data trends are quite spiky, especially in earlier years, due to effects of successive devaluations, which reduce the value of the denominator (GDP) and hence increase the weight of the deficit (or surplus) in dollars relative to GDP converted into dollars. Working against this, however, is the fact that domestic price inflation was higher than international price inflation in both South Korea and Brazil from the 1950s to the 1980s, thereby appreciating the converted value of GDP before and after devaluations. These considerations continued in the case of Brazil well into the 1990s, particularly given that the country reissued its currency on several occasions following the debt crisis of the 1980s in attempts to deal with hyperinflation. Nonetheless, bearing with this spikiness in the interpretation of the historical trends is arguably the least worst option for dealing with such data issues.

2.1 The case of South Korea

The case of South Korea, viewed through this balance of payments history, clearly demonstrates the crucial role that aid played in buttressing rapid late industrialisation against structural financial vulnerabilities. In this respect, it very much confirms the structuralist position discussed in the previous section.

The first and most striking feature of South Korea's current account in the first three decades of the post-war era was the consistent and very deep merchandise (goods) trade deficits right up until the early 1980s. This was the case even despite rapidly increasing exports throughout these decades and the shift to a greater emphasis on export-led industrialisation in the 1960s. The country only achieved a surplus on the merchandise trade account for the first time in 1986, although this was due to a major deceleration of both export and import growth between 1981 and 1985 (more on this below) due to the

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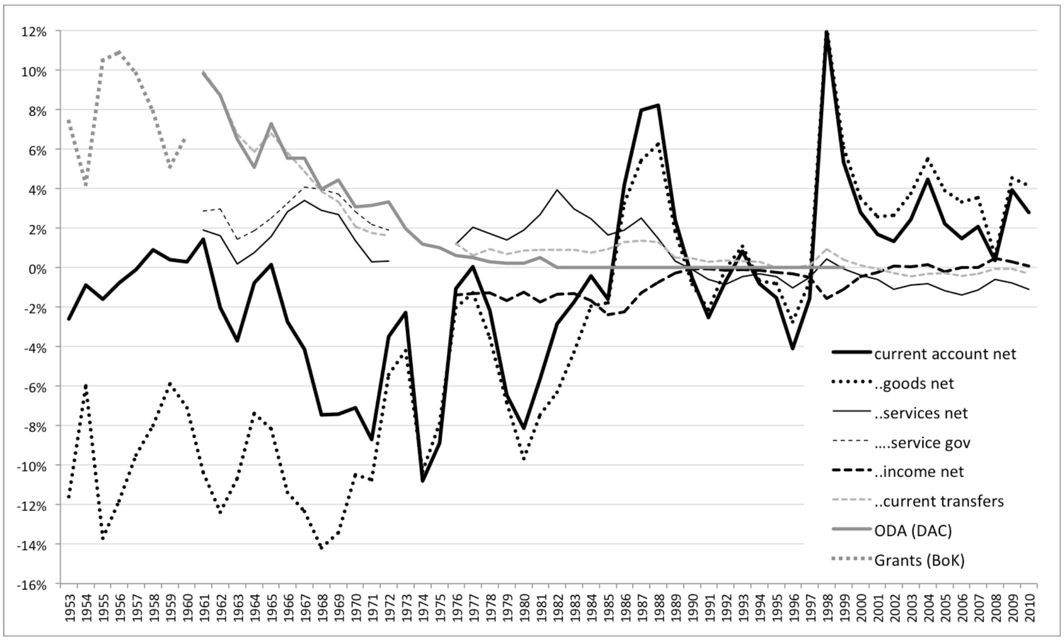
[29] Similar argument could be made with respect to the use of PPP conversions in measurements of international inequality. PPP conversions effectively compress the impression of inequality across more expensive (e.g. Japan) and less expensive (e.g. India) countries, in comparison to the value of local economies and incomes relative to their international purchasing power. International migrants are very aware of this difference, to the extent of living in dismal conditions in expensive cities for the sake of earning low wages in hard currency to send back home. So should we.

stabilization programme implemented during that time.[30] Keeping in mind the accentuated appearance of volatility due to successive devaluations, the merchandise trade deficit was consistently in the range of eight to twelve percent of GDP from the 1950s up to early 1971, when it was still at 10.7 percent. It fell again to 10.3 percent in 1974 and 9.7 percent in 1980. The deficit was never less than six percent of GDP until 1972 and it fell to 14 percent of GDP in 1968, in the midst of the country's take-off to an export success story. The choppy improvements to the deficit in the 1970s – counter-intuitively in the midst of the oil price shocks – were achieved through two stabilisation programmes, one in 1971 and another in 1974, although the effects were short lived.[31] In effect, both the remarkable take-off of exports during the 1970s and the shift into heavier and more capital intensive industries accentuated import demand rather than alleviating it.

FIGURE 1
South Korea Current Account and ODA, % of GDP (current values), 1953-2010



Source: calculated from IMF BoP data for 1976 onwards; Rhee (1973) for 1961-72; and BoK (1995) for 1953-60 and current and goods accounts for 1973-75.

From a comparative perspective, these merchandise trade deficits were far greater than those of Latin American countries up to the eve of the 1982 debt crisis, as discussed below in case of Brazil, which is testament to the fact that South Korea was much less constrained in its ability to run these deficits. This ability to run such deficits for such a sustained period of time is arguably an overlooked but important part of the country's development success story, at

[30] See Amsden (1989) for a discussion of these stabilization programmes.

[31] Amsden (1989, p.99) argues that the economy was in good shape prior to the second oil price shock in July 1979 based on the almost balanced current account from 1976 to 1978, although from the longer historical perspective presented here, this balance was very short lived and was an exception rather than the norm.

least in terms of removing obstacles that could have otherwise stunted or derailed rapid industrialisation strategies. Indeed, from the perspective of the net balances, there is no evidence of a shift from import substituting to export oriented strategy in the 1960s (although there is more evidence of this in the gross flows, as discussed below). Rather, to the extent that there was a shift in strategy,[32] export orientation proved to be as import intensive as the previous regime.

Moreover, the merchandise trade surplus that briefly emerged in 1986 was in response to the debt crisis and stabilisation, when the economy fell into recession. Imports in particular stagnated in 1982-83 and again in 1985, and the huge surge in the merchandise trade surplus from 1986-89 was associated with efforts to repay the debt that was accumulated to weather the crisis (shown in figure 2). Nonetheless, the surge was short-lived, even though it earned South Korea the reputation of a mercantilist nation, and then the economy returned to a pattern of deficits (albeit more minor) up until the East Asian crisis of 1997-98. A similar merchandise trade surplus surge occurred after this crisis and it is only at this point that economy sustained these surpluses even once the crisis subsided. While the most recent period is beyond the scope of this article, the country's development transition is nonetheless striking when observed through this long-term historical balance of payments lens.

The second striking feature of the South Korea's current account is that aid covered most of the merchandise trade deficits up to the early 1960s and made major contributions to balancing the current account well into the 1970s (especially depending on how liberally aid is defined). Grants alone (according to the BoK data) covered almost the totality of the merchandise trade deficit from 1956-60 and ODA (according to the OECD data) in 1961 was 9.8 percent of GDP, still almost completely balancing the merchandise trade deficit worth 10.4 percent of GDP. ODA gradually tapered off during the 1960s (in particular relative to the extremely deep deficits during the late 1960s) although it still accounted for about half of the merchandise trade deficit in the second half of the decade, e.g. ODA was 7.3 percent of GDP in 1965 for a deficit of 8.2 percent, 5.5 percent versus 11.4 percent in 1966, or 4.4 percent versus 13.4 percent in 1969. Even by 1972, ODA briefly accounted for more than half of the merchandise trade deficit (3.3 percent versus 5.4 percent), thereby providing crucial support to the first stabilisation programme in 1971. It fell below one percent of GDP from 1976 onwards, and dwindled to almost zero after slight jump to 0.5 percent of GDP in 1981 (from 117 million USD in 1980 to 326 million in 1981). ODA then turned slightly negative from 1984-86 and again from 1993 onwards (except in 1995), until the series is discontinued in the OECD DAC database after 1999.

Current transfers are also shown in figure 1 as an alternative to the DAC data and these data show similar patterns. The current transfers balance corresponded very closely with the DAC data through to the mid-1960s, was less in surplus than the DAC data in late 1960s and early 1970s, exceeded the DAC data after the mid-1970s, and then turned negative for the first time in

[32] As argued by scholars such as Amsden (1989; 2007) or Chang (2003), the industrial strategy is better characterised as having been a combination of both ISI and export orientation.

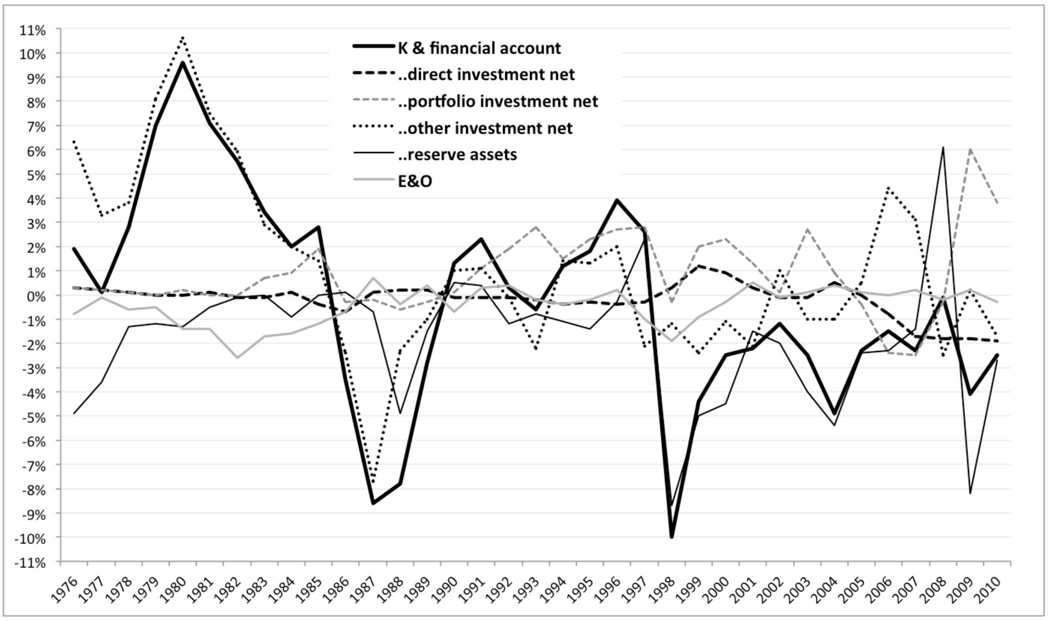
2001. As noted above, disaggregated data for the current transfers account was not available for the earlier period, although we can speculate that the differences might have been due to the way that concessional official loans are reported as ODA in the DAC data but not as part of current accounts, and hence as long-term concessional loans started to replace grants in the later 1960s, current transfers appeared lower than DAC ODA data. However, this does not explain the discrepancy in the 1970s, when current transfers started to exceed ODA, even while loans increasingly displaced grants (as discussed in the next figure). We can again speculate that the concessionality of many of the official sources of South Korean external debt in the 1970s was not sufficient to be counted as ODA, even if they were relatively more secure and long term compared to the commercial lending to Latin America during the same period (see below). In addition, there would have been an increasing role of workers' remittances on the current account. Similarly, entry into negative territory from 2001 onwards probably reflects a reversal in net migrant remittances as well as South Korea's transition from being a recipient to being a donor country.

The ODA data also do not capture several other important external channels supporting direct redistribution to the South Korean economy, even if not strictly defined as aid. One of these was the services trade balance that, unlike most developing economies, was running strong surpluses right up until the late 1980s. It was consistently in the range of one to four percent of GDP during these years, notably hitting peaks of 3.4 percent in 1967 and 3.9 percent in 1982. As can be observed in the earlier data from 1961 to 1972, this was entirely due to government services, whereas private services were in deficit during those years, as is typical for peripheral developing countries, e.g. see the case of Brazil below or China in Fischer (2010). The government services mostly represented the servicing of the US military, both in South Korea and in various ventures in South East Asia (Rhee 1973). As such, they were a lucrative form of income earned through generous contracts with the US government that can be considered as an implicit form of aid,[33] particularly considering the substantial role they played in balancing the current account. This was especially important as the role of grants was diminishing, e.g. government services were equal in proportion to ODA in 1968. This observation obviously highlights the geopolitical importance of South Korea (and Taiwan) for the US and their exceptional circumstances that drove both aid and US complicity with industrial policy.

The financial account data supplement these insights with an even fuller picture of the generous financial circumstances that were supporting the South Korean experience, particularly as the economy became more vulnerable in the 1970s. These are shown in figure 2, based on the IMF data from 1976 onwards. The financial account data in Rhee (1973) are not consistent with the more recent IMF reporting and hence are not shown, although the earlier FDI data is referred to below. The sub-accounts presented are also selective, in the sense that they do not include the net financial derivatives account.

[33] It is notable in this regard that Pentagon procurement has also served as a central albeit discrete and somewhat disguised tool of industrial policy in the US, e.g. cf. Vernon, 2006; Block, 2008; Mazzucato, 2013; Wade, 2014.

FIGURE 2
South Korea Financial Account, % of GDP, 1976-2010



Source: calculated from IMF BoP and IFS data.

Two main insights can be derived from these data, one on the important role of debt and another on the insignificance of FDI up to the 1980s. In the first case, as aid tapered off from the mid-1960s onwards and especially in the 1970s, it was replaced by debt as the main means of financing trade deficits (Rhee 1973). This trend can be seen in large surge in 'other' investment (i.e. bank loans) in the second half of the 1970s, besides in 1977 when current account was briefly balanced. Most of the movement on the overall financial account at this time was due to borrowing and, as discussed by Amsden (1989), this was an explicit government strategy to finance current account deficits, hence the very close correspondence. According to Rhee (1973, p.11), debt was at first dominated by long-term concessional loans from the US and then increasingly Japan, but then the structure of debt became increasingly composed of private short-term loans in the 1970s (debt was almost entirely long-term up to 1967). Nonetheless, private financial markets still only provided one third of total public external debt by 1978, whereas official sources provided close to half, in contrast to Latin American countries where the proportions were generally the inverse.[34] According to BoK data, this balance of official to private sources remained more or less the same up to 1985 (BoK 1995, p.756). Considering that the public external debt load in 1978 was much greater in South Korea than in Brazil or Mexico, whether measured

[34] See Frieden (1981); Mexico provides the strongest contrast to South Korea, whereas Brazil was between the two. For instance, official sources provided 45 percent of South Korea's total public external debt in 1978 and financial markets provided 33 percent (suppliers made up the remainder). In Mexico (same year), official sources accounted for about 20 percent and financial markets for 79 percent. In Brazil, official sources provided 31 percent and financial markets provided 56 percent (calculated from ibid. p.414).

relative to GDP or in per capita terms,[35] such generous supplies of official lending obviously played an importantly role in the resilience of South Korea through the subsequent financial crisis of the early 1980s. In particular, the less flexible interest rates on the official long-term loans would have tempered the impact of sharply rising interest rates from the late 1970s onwards.

Moreover, this supply of credit was crucially sustained throughout the 1982 debt crisis, whereas it dried up in Latin America (indeed, this was one of the triggers for the crisis in Latin America). The sustained supply of finance undoubtedly helped to stave off default, particularly in light of the very deep merchandise trade deficits, which remained at 6.3 percent of GDP in 1982 (and matched with a surplus of 5.9 percent on the other investment account). The substantial degree of capital flight is also significant, reflected by the deficit on the errors and omissions of 2.6 percent of GDP in 1982 (it again reached 1.9 percent of GDP in 1998). This qualifies the argument that South Korea escaped the crisis because its loans were predominantly long term with fixed interest rates, whereas those of Latin America were short term with flexible interest rates, as noted above. The sustained supply of foreign finance throughout the otherwise financially austere conditions facing the rest of developing countries appears to have been an equally if not more crucial factor preventing debt crisis in South Korea. In any case, both the supply and structure of external debt reflect the preferential conditions accorded to South Korea, allowing its industrialisation trajectory to persevere rather than be crippled.

The tight correspondence between debt, the overall financial account balance, and the current account subsequently broke down following the post-1982 crisis surge of the current account surplus, which was evidently associated with the repayment of debt. The rupture was first marked by a brief spell of reserve accumulation and then by the increasing prominence of portfolio and other financial flows in the 1990s (derivatives are not shown in figure 2). Reserve accumulation subsequently became the main determinant of the financial account following the East Asian crisis, particularly as stabilisation and austerity again threw the economy into a surplus overdrive on the current account. The latter reached 11.9 percent of GDP in 1998 and was compensated by a deep financial account deficit of 10 percent of GDP, most of which was determined by the reserve account, at 8.7 percent of GDP, rather than by debt deleveraging (although the latter was nonetheless significant). The pattern by which reserves largely determined the financial account only emerged after this point, at least up until the 2007-09 global financial crisis, as was common across most 'emerging' and developing economies.

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[35] According to Frieden (1981, p.414), the public external debt of South Korea in 1978 amounted to just over 18 billion USD, whereas Mexico's was 27 billion USD and Brazil's was just under 32 billion USD (less than double). In comparison, South Korea's GDP was approximately 50 billion USD, whereas Brazil's was 200 billion USD (four times) and Mexico's was approaching 200 billion. South Korea's population was about 37 million, Mexico's about 70 million, and Brazil's about 93 million. Obviously, these measures of public external debt would not include privately contracted debt, much of which was socialised in Latin America following the 1982 debt crisis.

The second important insight is that net FDI remained very marginal up to the 1990s. Based on data from Rhee (1973) – not shown in figure 2) – net FDI was almost non-existent prior to 1966. Thereafter it remained well below 0.5 percent of GDP up to the 1990s, besides in a few exceptional years (e.g. it reached 0.6 percent in 1971) and it was often slightly negative in the 1980s. These net flows more or less represent gross flows of foreign direct investment into South Korea up to that time given that there were effectively no outflows of direct investment abroad prior to the 1980s. This confirms the observation – seminally emphasized by Amsden (1989, p.21) although underemphasised in much of the subsequent literature – that South Korean industrialisation 'occurred almost exclusively on the basis of nationally owned rather than foreign-owned enterprises.' She notes that South Korea relied on 'massive imports of foreign licenses and assistance' as a means to attain technological independence and to avoid foreign control, which was preferred 'to depending on foreigners to run Korean plants' (ibid. p.20-21). Notably, such modes of technology acquisition would be recorded on the private services account rather than as FDI on the financial account, and were primarily financed through external debt, particularly as aid tapered off in the 1960s and 1970s.[36] Even during the peak net inflows of FDI following the East Asian crisis, which caused lots of political controversy in South Korea, net FDI nonetheless only briefly amounted to 1.2 percent of GDP in 1999 and 0.9 percent in 2000. It subsequently turned negative in 2000s, representing net direct investment outflows by Korean corporations or by foreign affiliates that had been established in South Korea in the 1990s and that were using the country as a first tier platform within regional production networks.

In sum, the external accounts of South Korea reveal several attributes that do not necessarily explain the industrial success of country, but that definitely highlight how certain decisive constraints on this industrial success were relaxed over several decades of intense and vulnerable transformation. One is an exceptional ability to run merchandise trade deficits. Second is that these were financed first through aid (for the good part of 20 years) and then through debt, the bulk of which was official well into the 1980s. Given the magnitude of aid in the 1950s and 1960s, it is difficult to imagine how South Korea would have been able to pass through the early stages of its industrial transformation without such assistance, at least not without much more constrained trade deficits, which would have arguably curtailed industrialisation, and/or with much greater degrees of FDI and volatile forms of private financing, as was the case in Latin America. Even when aid was dwindling in the 1970s, indirect assistance through government service provisioning to the US military in Asia, together with guaranteed supplies of long-term loans first from US and increasingly from Japan, and preferential trade access to US markets, all contributed to relaxing constraints and providing stability in the 1970s. Even despite this direct and indirect aid in the 1970s, the South Korean economy increasingly relied on short-term

[36] Amsden (1989) elaborates, for instance, that domestic savings (and especially household savings) in the 1960s were never close to being able to satisfy investment demand (p.74), and government deficits in the late 1970s, due to high levels of investment into and operation of public-sector enterprises, were similarly financed by borrowing (p.89-90).

commercial lending and also ran into serious difficulties and imbalances in the late 1970s and early 1980s, like in Latin America. However, debt did not dry up in the context of the 1982 international debt crisis, despite the exceptional current account deficits that South Korea was running up to the crisis – far deeper than those observed in Latin America – which under normal circumstances would have given financial markets cause for concern. The maintenance of these implicit forms of assistance was crucial to the stability of South Korea during this profound global crisis that caused upheaval in Latin America and Africa.

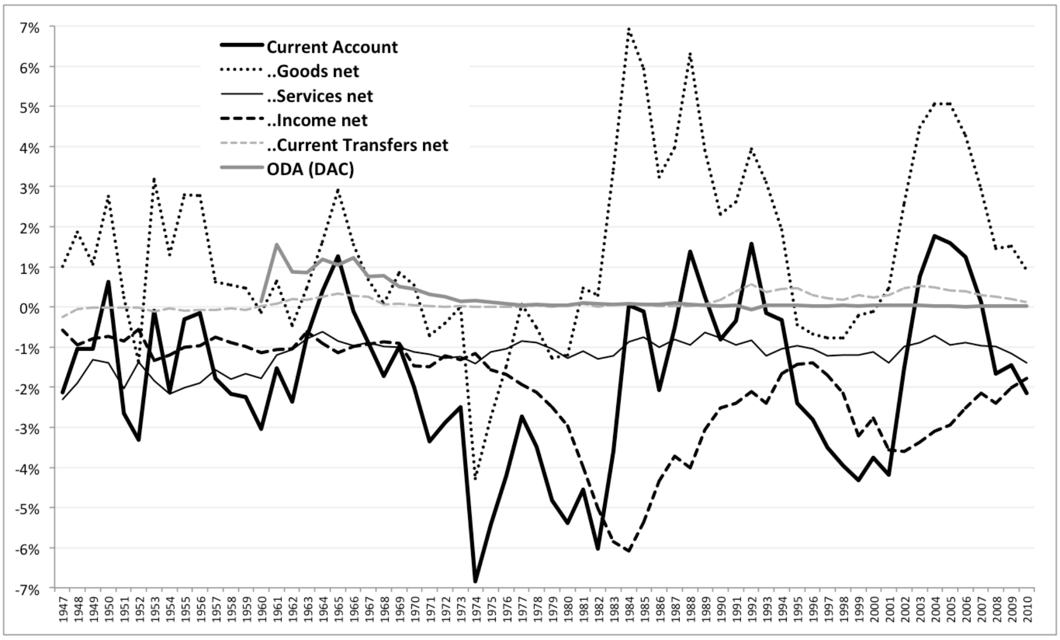
Without denying the other important elements of South Korea's success, as amply dealt with in the literature (e.g. industrial policy, land reform, and a strong developmental state able to implement plans and to discipline capitalists), it is evident how the South Korean model would have been destabilised towards a path more akin to the Latin American experience in the absence of huge levels of aid and other forms of assistance. The argument that aid *alone* caused South Korea to emerge from its 'poverty trap' obviously does not hold water. However, aid definitely played a key role in allowing the country to pass through several very vulnerable stages of its intensive industrialisation. Without aid, it is plausible that chronic balance of payments crises would have choked the potential provided by the other more domestic and productionist elements contributing to South Korea's success.

2.2 The case of Brazil

In contrast to South Korea, the case of Brazil clearly demonstrates the constraints faced by late industrialising countries in the absence of generous supplies of aid and/or stable, secure and affordable finance. Brazil's only exception to this rule was during the 1970s, when the country did face generous financial conditions and its external accounts manifested patterns similar to South Korea. However, these were forcefully reversed following the 1982 debt crisis, to such an extent that the structure of Brazil's external accounts ended out exhibiting, circa 2010, the same structural patterns as in the early post-war period. The productive foundations of the Brazilian economy had obviously fundamentally changed, in terms of the depth and extent of industrialisation that the country did manage to achieve over these seven decades. Nonetheless, viewed purely from the perspective of the external accounts, the beginning and end of this period exhibited a similar structural predicament of merchandise trade surpluses and private financial inflows financing overall current account deficits, the latter due to large deficits on both the services and income accounts.

The failure to break out of this predicament is clearly evident in the current accounts data shown in figure 3, particularly when viewed in comparison to the data for South Korea in figure 1. Brazil started the post-war period in a classic peripheral pattern of external integration as stated above (indeed, it was this pattern that inspired much of early structuralist analysis, such as in the work of Prebisch). It ran merchandise trade surpluses for the first decade and a half, with the exception of 1952 when balance of payments problems forced the introduction of a multiple exchange rate system (replacing fixed exchange rates). The services account deficits were largely due to items that were in mostly foreign control, such as transport, finance, insurance, and royalties, while the income account was mostly composed of remittances of profits on foreign investment and interest payments on debt. The deficits on these two accounts exceeded the merchandise trade surplus and, as a result, the overall current account was in deficit throughout most of this period. However, this overall deficit was fundamentally different from that of South Korea in that it was not driven by an excess of merchandise imports and it was financed through a variety of private financial channels such as FDI, loans and 'other operations', as shown in figure 4. As noted in the previous section, it was precisely this situation that inspired early structuralist authors such as Prebisch and Furtado to focus on the import austerity that chronic balance of payments constraints imposed on industrialisation efforts.

FIGURE 3
Brazil Current Account and ODA, % of GDP (current values), 1947-2010



Source: calculated from data appendices in Giambiagi et al (2011).

The structure of the current account was essentially the same in 2010 and in most of the intervening years besides during the 1970s. By 2010, the surplus on the merchandise trade account only financed part of the services and income deficits, resulting in an overall current account deficit. To put this in nominal terms, Brazil had a 20 billion USD merchandise trade surplus in 2010, matched by a 30 billion USD services deficit and a 37 billion USD income account deficit, for an overall current account deficit of close to 47 billion USD. As shown in figure 4, this was financed through net financial inflows of about 100 billion USD, half of which went into reserves. In the context of global economic slowdown from 2013 onwards, the merchandise trade account went into deficit in 2014 due to a reduction in the value of exports and a corresponding stagnation in imports, highlighting the predicament of non-developmental trade deficits, versus deficits that result from imports increasing faster than exports.[37] Despite radical transformations of the economy during these seven decades (e.g. substantial industrialisation and financialisation), the lack of transformation in the structure of the external accounts is suggestive of certain fundamental structural predicaments that had not been overcome and, in certain respects, might have even intensified (such as the presence of foreign ownership, as highlighted in the early dependency literature).

It is also evident that the current accounts of Brazil were much more constrained than those of South Korea. The country was only able to run sustained merchandise trade deficits from 1971 to 1980, and then very mildly from 1995 to 2000 parallel to the large surge of FDI that lasted from 1996 to 2001. However, these deficits were only minor contributors to the overall current account deficits, given the ongoing chronic deficits on the services and income accounts (versus South Korea, where the merchandise trade deficits exceeded current account deficits and were compensated by the services account). Moreover, these deficits only ever exceeded one percent of GDP on a few occasions (in 1952, 1974-76, and 1979-80), and more than two percent only in 1974-75 (e.g. the merchandise trade deficit briefly reached 4.3 percent of GDP in 1974). Indeed, Brazil was already running a small goods surplus in 1981, the year before the debt crisis, due to an austerity programme that was already aimed at keeping the IMF at bay.[38]

The oil shocks are usually suggested as an explanation for merchandise trade deficits in the 1970s. However, the increase in oil and related imports actually only accounted for a minor share of the overall increase in merchandise imports between 1972 and 1974, and capital and intermediate goods still accounted for almost three quarters of merchandise imports in 1974, when the merchandise trade account fell into its deepest ever deficit (see data in Giambiagi et al 2010, p.254). While oil imports became more important later in the decade, reaching half of all merchandise imports by 1981 and contributing to the merchandise trade deficits in late 1970s, the more significant explanation for the deficits (and for increased oil consumption) was the strong move into second stage ISI policies from the late 1960s onwards, as a means to intensify industrial upgrading and diversification into heavier and more technologically complex industries, famously characterised by Castro and Souza (1985) as the *Marcha Forcada*. Brazil took advantage of the generous and affordable supply of external loans for this purpose, much like South Korea although with a greater reliance on commercial sources, as discussed above. The industrial strategy was similar to that of South Korea, although unlike South Korea, import capacity in Brazil was eroded rather than enhanced by the services deficit.

Moreover, the deficit on Brazil's income account by the end of the 1970s had worsened to a far greater extent than in South Korea, which is again reflective of the longer-term external debt structure of South Korea and the preferential geopolitical conditions that allowed for this. Notably, the income account deficit of Brazil had become a far more powerful factor driving the

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[37] The result in 2014 was a current account deficit of 104 billion USD, financed by an inflow of 100 billion USD on the financial account (of which 77 billion was from net FDI), with the remainder covered by a reduction in reserves.

[38] See the contemporaneous reflection on this period by Diaz-Alejandro (1983).

current account deficits at that time than oil imports. As a result, the overall current account of Brazil remained deep in deficit despite the small goods surplus in 1981-82 and reached six percent of GDP in 1982, due to a rapidly worsening deficit on the income account that was increasingly dominated by interest payments on short-term commercial debt. In this era of high interest rates that ushered in and followed the crisis, the deficit on the income account remained by far the strongest negative pull on the overall current account.

Meanwhile, the economy was quickly adjusted to generate very large merchandise trade surpluses, which reached almost seven percent of GDP in 1984, in order to finance these income account deficits and to balance the current account (which Brazil managed to do in 1984). This surge was seminally discussed by Diaz Alejandro (1984), who explained how most Latin American economies were able to generate merchandise trade surpluses very rapidly after the advent of the debt crisis by essentially crippling their economies through combinations of severe austerity and/or sharp devaluations, both of which sharply reduced imports rather than increasing exports. Indeed, the capacity to increase exports – beyond the vagaries of terms of trade – was severely constrained by both the investment and import austerity imposed by the stabilisation programmes. This is definitely observed in Brazil, where imports fell from a peak of 23 billion USD in 1980 to a trough of 13 billion USD in 1985. Exports experienced substantial volatility, increasing above the 1981 peak of 23 billion USD in 1984-85, but falling below this earlier peak in 1986, and then increasing again thereafter. The initial surge of exports following the crisis was almost entirely due to the export of manufactures (e.g. see Giambiagi 2010, p. 253). Castro and Souza (1985) argued that this initial success in weathering the crisis, particularly in contrast to other Latin American countries, was in large part attributed to the intensive ISI policies followed in the 1970s. Nonetheless, this initial success was undermined by the severe import austerity, which more than halved the import of capital goods and almost halved the import of intermediate goods from 1980 to 1984 (Giambiagi et al 2011, p.254). In contrast and as discussed above, imports in South Korea stagnated but did not collapse over these years, and the turbocharge into generating trade surpluses was also delayed until later in the decade, under more advantageous external circumstances.

Instead, Brazil (and other Latin American countries) was forced to bear the full brunt of stabilisation and adjustment in the peak of the crisis when circumstances were at their least advantageous. The strain that austerity, stabilisation and adjustment placed on the Brazilian economy is notably reflected by the fact that annual consumer price inflation surpassed 100 percent for the first time in 1980, surpassed 200 percent from 1983 to 1985, then 400 percent in 1987, and over 1000 percent from 1988 to 1990 and again from 1991 to 1994 (ibid. 247). Inflation occurred in tandem with a series of spectacular devaluations from 1980 to 1988 and the issuing of successive new currencies, finally ending with the Real in 1994. In other words, the government was able to structurally adjust the economy into an emergency mode of generating large trade surpluses, principally for the purpose of paying off the debt burden, although this exacerbated other disequilibria of the economy, as classically highlighted by Prebisch.

In addition to these trade considerations, Brazil also lacked the major contribution of aid to compensate the income and non-government services deficits on its current account, as had been the case for South Korea up to the 1970s. It should be noted in this regard that the ODA data from the DAC sources do not correspond with the current transfers account data from the Brazilian balance of payments. This might be explained by the fact that much of the ODA recorded was in the form of concessional loans, which would not have been recorded on the current transfers account.[39] In any case, if we rely on the DAC data, there was a minor surge of ODA in 1961, to 1.5 percent of GDP, which was sustained at just above one percent of GDP from 1964-66, during the first years of the US-allied military dictatorship. ODA then tapered off to an insignificant level by the 1970s, in particular relative to the deficits on the other current accounts.

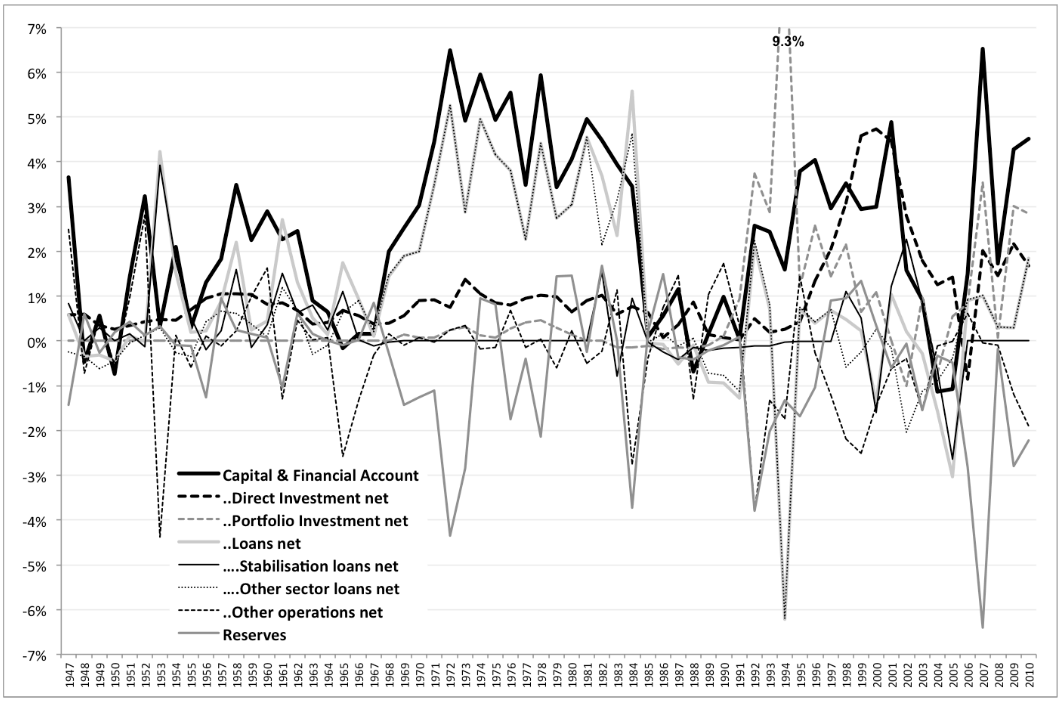
Moreover, in all of the years (besides 1962) when ODA was strongest (e.g. at 0.5 percent of GDP or more), the country was actually running merchandise trade surpluses. Therefore, unlike South Korea, aid was not financing net merchandise import capacity but, instead, was financing the services and income deficits (in a macroeconomic sense). Indeed, aid made a significant contribution to achieving overall current account surpluses in 1964 and 1965, and a near-surplus in 1966, although this contribution was accompanied by a strong surge in the merchandise trade surpluses during those years, achieved through temporary import austerity.[40]

In contrast to the short episode of aid inflows, the more regular, stable and sustained source of foreign funding throughout the entire period came from net FDI, as shown in figure 4. However, despite the emphasis that FDI received in the earlier dependency literature, net FDI rarely exceeded one percent of GDP. It only surpassed two percent of GDP during the exceptional surge in the late 1990s, when FDI reached almost five percent of GDP from 1999 to 2001, which was apparently related to the privatisation of publically-owned entities, particularly in telecommunications and electricity (OECD 2000, p.35). Nonetheless, the more generalised levels of FDI were sufficient to establish the dominance of foreign corporations in key strategic industrial sectors, such as the automobile industry where foreign-owned firms accounted for 92 percent of sales by 1995 (Chudnovsky and López 1997, cited in Baumann 1999, p.11).

[39] Other possible explanations include: the opacity and questionable quality of the government's accounts in this period (e.g. see a discussion of this in Diaz-Alejandro 1983); the fact that other types of current transfers (such as workers remittances or 'other transfers' out of Brazil) were cancelling out the inflows of aid; or else the perennial problem of the aid system whereby much of the assistance reportedly given to a country is not actually transferred to that country, but instead remains in the donor country through various practices of technical assistance, contract tendering, and so forth.

[40] Gross merchandise imports fell from about 1.3 billion USD in 1963 to 0.9 billion USD in 1965, and then recovered to 1.3 billion USD in 1966. Interestingly, South Korea experienced similar import austerity in the same years, with gross merchandise imports falling from 497 million USD in 1963 to 365 million in 1964, and then recovered thereafter.

FIGURE 4
Brazil Financial Account, % of GDP, 1947-2010



Source: same as previous figure.

Moreover, as argued by Sunkel (1972), TNC subsidiaries could expand by drawing on domestic sources of finance, thereby not necessarily requiring additional injections of FDI in order to finance further domestic expansion. Indeed, the subsidization of TNCs by ISI policies in Brazil and other Latin American countries was a central point in the dependency critiques of ISI by both Sunkel (1972) and Furtado (1973). To the extent that their prognosis was correct, the limited degree of FDI that was required to produce such conditions is striking and highlights the consequences of the much greater weight of FDI since the mid-1990s. As discussed above, it also contrasts with South Korea, where industrialisation occurred on the basis of mostly national ownership. The scale of FDI in both cases also puts into perspective the role of FDI in the post-1992 experience of China, where net FDI (as a proportion of GDP) was sustained for about two decades at the levels briefly reached in Brazil in the late 1990s.[41]

Another point worth noting on the financial account of Brazil was the limited role of commercial borrowing up until 1968. This reflects the very constrained private financing options generally facing developing countries in the early post-war period, in contrast to the much more generous conditions facing South Korea up to the explosion of international lending from the late

[41] Net FDI to China consistently amounted to three to six percent of GDP from 1993 to 2000, and then from two to four percent from 2001 until 2010, with the exception of 2009, when it fell to 1.4 percent. As a result, foreign-funded corporations quickly came to dominate the export sector in the 1990s and then the merchandise trade surplus in the 2000s (see Fischer 2010 and 2015; also see the conclusion for further discussion on the China comparison).

1960s onwards. Prior to 1968, the financial account of Brazil was largely determined by volatile movements of 'other operations' on the 'other investment' account (as per the terms used by Giambiagi et al 2010),[42] and by stabilisation loans (i.e. from multilateral institutions such as the IMF).

In the case of other operations, the only significant non-loan category of other investments would have been cash and deposits, given that international derivatives, repos, and other such financial innovations essentially did not exist in the early post-war period. The volatility on this account appears to have been the primary determinant of financial instability up to the mid-1960s, swinging from a surplus of 2.5 percent of GDP in 1947, to a slight deficit in 1948, to a surplus of 2.8 percent in 1952 and then a deficit of 4.4 percent of GDP in 1953. These levels were in a similar magnitude as the overall current account deficits and the services account deficits, although considerably more volatile. They are suggestive of the deep integration of the Brazilian economy and elites into the international (and especially US) financial system, even if through the more traditional financial routes of cash and deposits, particularly in the immediate post-war period when the government adopted a free trade regime with fixed exchange rates, which ended with the balance of payments crisis in 1953.

In the case of loans, most net borrowing was in the form of stabilisation loans up to 1968. This corresponded to the succession of balance of payments crises in 1953, 1958, 1961 and 1965, after which Brazil was able to avoid recourse to such emergency financing until 1982. Notably, this series of balance of payments crises in the 1950s was the thorn of contention in the then-famous debates between the structuralists and monetarists in Brazil,[43] and were the impetus behind the earlier articulations of dependency theory from within the CEPAL school of structuralism, as discussed in the first section.

2.3 Gross merchandise trade flows compared

As a final comparative perspective, it is insightful to examine the weight of gross merchandise trade flows relative to the domestic economy of both cases (presented in figure 5 with data up to 1994). As has been well recognised, South Korea ended this period with a much stronger weight of exports in its economy than Brazil. This differentiation became apparent in the mid-1960s, as the remarkable rise of gross exports to GDP that started in 1960 in South Korea contrasted with the gradual albeit punctuated decline in gross exports to

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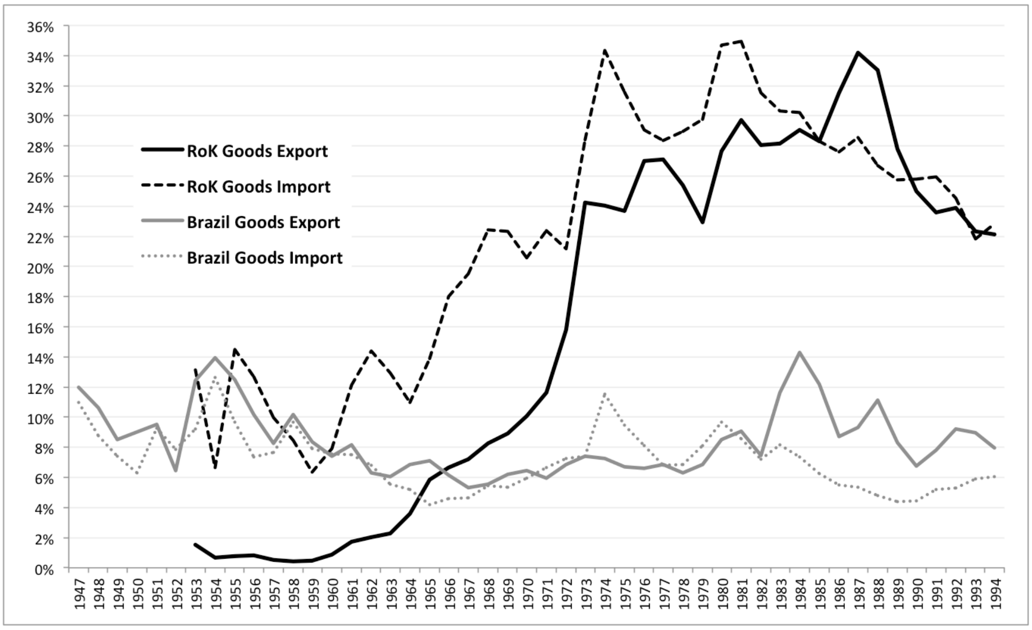
[42] Giambiagi et al (2010) disaggregated the 'other investment' category into 'loans' and 'other operations'.

[43] Notably, despite the common caricature of this earlier period as 'structuralist' in much of the contemporary literature, the monetarists generally dominated over the course of policy, in terms of the nature of stabilisation programmes adopted and subsequent policy approaches, even if they did not necessarily win the intellectual debates. As argued in Fischer (2015, p.710), the epochal appellation is more appropriate for representing the more mainstream structuralism of US economists such as Hollis Chenery, and the World Bank under his leadership. The early Latin American structuralists placed much greater emphasis on the need for radical redistribution and deep structural transformations in order to overcome the very polarised nature of Latin American economies that manifested in these macroeconomic disequilibria.

GDP in Brazil from the late 1940s up to the late 1960s (albeit from a higher starting point – Brazil started the post-war period more export oriented than South Korea). The transition point, when the ratio of gross exports to GDP for South Korea surpassed that of Brazil, occurred in 1966. The bulk of the increase in South Korea's ratio occurred up to the mid-1970s, from just under one percent of GDP in 1960, to 10 percent of GDP by 1970 and then to over 24 percent of GDP by 1973. This increase was accentuated by regular devaluations occurring up to 1975 (and then continued in 1980), although it nonetheless represents remarkable increases in the USD value of gross exports. In contrast to Brazil's economy remained much more domestically oriented, besides during the short-lived surge following the 1982 crisis, when gross exports reached 14 percent of GDP in 1984.

FIGURE 5
Gross merchandise trade, Brazil and South Korea, % of GDP, 1947-1994



Source: same as previous figures.

The weight of gross imports to GDP, however, was equivalent in both economies up to 1960, and it is notable how the export surge in South Korea was preceded by an even greater surge of imports. Gross imports as a ratio of GDP reached 22 percent already by 1968, 34 percent by 1974, and then a peak of 35 percent by 1980. The contrast with Brazil is suggestive of the argument that it was the constrained capacity to import that impeded the ability of Brazil to develop its manufacturing exports further or faster than it did, whereas South Korea had much more generous circumstances in this regard, provided by aid and then preferential supplies of debt. At the very least, these structural distinctions need to be taken into consideration in comparative assessments of the two economies, rather than relying on purely domestic political economy considerations to explain differences in performance, such as greater or lesser policy preferences for import-substituting or export-oriented industrialisation policies, or differences in types of state organisation or intervention.

The nominal values underlying these proportionate gross flows provide further insights. Brazil quickly adjusted to the 1982 debt crisis through a drastic reduction in imports, as noted previously, whereas the simultaneous adjustment in South Korea (in imports as a proportion of GDP) at first did not generate a trade surplus and was not achieved by collapsing imports. Instead, the nominal value of imports in South Korea stagnated (but did not fall) at around 24 billion USD from 1981 to 1983, and then at around 27 billion USD in 1984-85. Moreover, when South Korea started to run merchandise trade surpluses for first time from 1986 to 1989, it did so while increasing imports, from 30 billion USD in 1986 to 57 billion USD in 1989. It is only by this time that the South Korean economy had truly managed to make a full transition to what might be called an export-driven economy, in the sense of exports leading the consumption of imports or at least increasing in synchronicity with them, rather than the financing of imports leading the capacity to export. In contrast, the import austerity associated with the apparent export orientation of Brazil in the 1980s ultimately undermined its export orientation in the medium term, particularly in manufactured exports.

3 Conclusion

The contrasting balance of payments histories of South Korea and Brazil highlight certain fundamental principles about the role of international redistribution in relaxing external constraints that are decisive for economic development, understood as centrally involving industrialization. This symbiosis between redistribution and development operates through the channel of trade deficits insofar as such deficits are both necessary for the absorption of redistributive flows and have been inherent tendencies of unconstrained post-war late industrialisation. Successful cases of such post-war late industrialization – here represented by South Korea – were externally supported in a variety of explicit and implicit ways in order allow for such deficits.

Aid effectiveness in this regard needs to be understood in terms of these two wings of redistribution and developmentalism, the latter essentially understood through the practice of industrial policy. The absence of the latter wing renders aid as welfare, which serves important purposes but should not be misconstrued as developmental. The absence of the industrial side of the equation in most of the contemporary aid literature is also an obvious elephant in the room, as is the absence of the redistributive from much of the political economy literature on industrial policy or developmental state capacity. Both lacunas risk overlooking the vital synergy between international redistribution and productionism operating in the most successful cases of post-war late industrialisation.

In the case of South Korea, aid and other implicit forms of support, including generous supplies of official finance, definitely played a key role in its rapid emergence as an industrial power well into the 1970s and arguably even into the 1980s. In particular, aid and debt permitted this emergence to occur without reliance on FDI and, hence, through mostly national forms of ownership. They allowed the country to run deep merchandise trade deficits throughout this entire period, to an extent never observed in Latin America, ironically despite the reputation of the country as an export-oriented poster child. The country did perform impressively in terms of increasing exports, but it was guzzling imports at an even faster pace and, in this sense, it had not solved the predicament faced by Latin Americans of an increasing import intensity associated with ISI policies, particularly as these shifted towards more capital intensive industries, at least not until the late 1980s. Rather, its capacity to increase exports was arguably permitted by its ability to increase imports, which was crucially funded by aid and other forms of support. The fact that aid was associated with such deficits also meant that aid absorption was not particularly problematic in a macroeconomic sense, although this was predicated on strong state-led industrialisation policies.

In the contrasting case of Brazil, aid was insignificant besides during a short spell during the 1960s. The spell, however, occurred in the context of merchandise trade surpluses and even reductions in the gross value of imports from 1962 to 1965. It was thereby rendered redundant in a macroeconomic sense, except by way of its contribution to counterbalancing the chronic services and income deficits, but not in terms of its role in enhancing the capacity to increase imports and to run development-induced merchandise trade deficits.

Moreover, in the absence of generous external funding conditions, Brazil's development strategies quickly become constrained by the inability to run sustained trade deficits. The resultant strains resulted in the succession of balance of payments crises in the 1950s and early 1960s, which were resolved through austerity and stagnation. Indeed, the punctuated attempts to run trade surpluses from the first crisis onwards were, until recently, the result of the austerity and stabilization programmes, with austere consequences for industrialization strategies. However, once these contractionary pressures on the economy were relaxed and industrialization strategies reinvigorated, the external constraints invariably re-imposed themselves, at least until they were relaxed by the explosion of international lending from the late 1960s onwards. External debt allowed Brazil to run sustained merchandise trade deficits for a decade and for the first time in the post-war period. The economy nonetheless reverted to the earlier dynamics following the 1982 debt crisis, when borrowing became much dearer. Although beyond the scope of this paper, a similar scenario is quite possibly occurring today, albeit with even deeper foreign ownership in the economy and even more volatile financial flows.

Beyond these vulnerabilities and crises, the external constraints faced by Brazil also accentuated other long-term perverse trajectories of development, such as polarisation and domestic macroeconomic instability, as classically argued in the structuralist economics literature. Indeed, even in the presence of generous supplies of external funding, South Korea was still under considerable strain through its dramatic and rapid transformation, to the extent that generous supplies of official lending were still central to the economy's stability up to and following the 1982 debt crisis. Brazil was much more constrained in this regard, with negligible aid and limited supplies of debt prior to 1968, most of which was in the form of official lending associated with the monetarist stabilisation programmes overseen by the IMF. The reliance on a regular inflow of FDI, alongside the volatility of other private non-debt financial flows, was undoubtedly encouraged by the economy's fairly liberal integration into the US-led world economic order as its starting point in the post-war era. The regular inflows of FDI nonetheless led to foreign dominance in the strategic lead industries of the country and also entrenched the structural pattern of deficits on the services and income accounts (whereas South Korea managed to attenuate the latter tendency by the 1980s, at least on the income account).

Overall, viewed from this long-term perspective, the current accounts of South Korea reveal a fascinating external view on its economic transformation. The current accounts of Brazil reveal a remarkable lack of transformation away from a pattern of external predicaments inherited from the early post-war period, despite quite deep structural transformations in the domestic economy. Brazil's predicaments are most quintessentially expressed in terms of merchandise trade surpluses financing services and income account deficits, with the net current account balance often in deficit and financed through expensive, volatile and regularly punitive private financial flows. While South Korea has also had to contend with an increasing inundation and volatility of private financial flows into its economy, particularly since the East Asian financial crisis, it did not have to confront these flows with the burden of the external predicaments faced by Brazil, whether at the beginning of the post-war period or at any point since. An important reason for this is arguably attributed to development space that aid provided, in synergy with the policies that actually took advantage of this space to produce development (i.e. industrialisation) outcomes.

Recognition of this symbiosis between redistribution and development has been mostly overlooked or ignored in the profuse aid literature, as well as in the parallel literatures focused on the political economy of development, such as on industrial policy and developmental states. One reason for this oversight is likely that the two literatures dealing with either aid or industrial policy (and developmental states) have tended to exist in separate non-communicating silos. In particular, the mainstream aversion towards industrial policy has caste a shadow over the donor-influenced aid literature for much of the last three or more decades. In riposte, this has encouraged cynicism towards the role of aid in the recent industrial policy literature (much of it rightly earned). There is also a (healthy) scepticism in the industrial policy or developmental state literature towards dominant discourses regarding the necessity of capital account openness in order to finance development, which in turn has encouraged a tendency to emphasise (perhaps overemphasise) a productionist reading of the East Asian development experience. Yet while it is true that FDI and other non-debt private financial flows were relatively insignificant in the macroeconomics of the South Korean experience, this is not to say that international redistribution and debt were also insignificant. Their role in the South Korean case is not to be underestimated.

The productionist emphasis has also been encouraged by the more recent experience of China, in which aid has been relatively insignificant, like in the

Brazilian case. The standard reading of China is one that endorses a 'boot straps' mentality to development and is often evoked in critiques of aid and in endorsements of FDI-led approaches to development. China also seems to repudiate the idea that running trade deficits is inherent to or necessary for late industrialisation, insofar as China has been industrialising rapidly and maintaining massive levels of investment while, at the same time, running large trade surpluses since the early 2000s. Notably, the option of using trade surpluses rather than deficits to fund rapid industrialization – through externally augmented demand rather than net financial inflows, as discussed by Kregel (2008) – has been a relatively new phenomenon among developing countries, dominated by the apparent exceptionalism of China since the late 1990s. Indeed, China seems to be the inspiration behind the 'Keynes-Schumpeter' hypothesis stipulated in UNCTAD (2008, p.69-70), which argues against the conventional wisdom that current account deficits are necessarily better for growth.

It is nonetheless important to recall, as argued by Fischer (2010; 2015), that China's balance of payments exceptionality has been so far short lived and we do not yet fully comprehend the consequences. It emerged in the early 2000s more or less as a mirror image of the equally exceptionally US descent into trade deficits. Before this time, China behaved like any other developing country; periods of spurting industrial growth led to both inflation and trade deficits, which in turn were only resolved through austerity. Aid was relatively insignificant and, in the absence of any other major sources of foreign finance, its ability to run trade deficits was effectively constrained, which was arguably an important factor spurring the policy of opening up to and strongly encouraging FDI in the 1990s. The last major trade deficit occurred in 1993 and its resolution occurred alongside an enormous surge of net capital inflows lasting from 1992-97, reinforced by an even greater surge of net capital inflows lasting from 2001-05, both of which were dominated by net FDI inflows, which were sustained for 15 years in the range of three to six percent of GDP. Such levels, sustained for such a long period of time, were much greater and longer than those observed in Brazil. They set China decidedly on its current path as mass global manufacturing hub, although a rarely acknowledged attribute of this path has been the rapid denationalisation of China's exports in the 1990s and of its merchandise trade surplus since the early 2000s. By 2012, 'foreign-funded enterprises' (mostly wholly foreign-owned) came to account for half of exports and two thirds of the merchandise trade surplus of China (Fischer 2015, p.723-4).

This sudden foreign domination of the suddenly ballooning trade surplus is reflective of the increasingly deep integration of China's foreign trade into international networks dominated by northern-based transnational corporations. The model has resulted in exceptional export performance, although this has occurred through relinquishing national control over the country's main means of earning foreign exchange. Combined with the surpluses on the financial account, which by definition represent foreign claims on domestic assets, China's equally rapid build up of reserves represents, to a large extent, the accumulation of foreign liabilities, as explained by Yu (2013). A corollary is that an important implicit channel for the entry and horizontal expansion of foreign corporations into the domestic economy of China has been through the trade account, rather than through the more restricted financial account, as was conventionally the case in Latin America and other regions. Hence, despite the evident achievements of China, its rise has exhibited vulnerabilities that are more peripheral than central in nature, albeit the precise mechanisms are quite different from the past, such as those operating in Latin America. In this respect, it has taken very strong interventionist measures to overcome the country's very real external financial vulnerabilities. These various tensions are arguably key to understand current political economy dynamics in China today, as well as the limited ability of the central government to balance the domestic economy.

Viewed through this prism, the case of China sends us back to the important lesson from the South Korean case, which is the preservation of national ownership of economic development through reliance on aid and debt rather than FDI or other forms of foreign investment. As once famously asserted by Lewis (1978), debt preserves sovereignty (so long as it can be managed), whereas FDI effectively denationalizes industrialization. The problem today is that the rich people and countries generally enjoy the cheapest financing, whereas the poorest generally only have access to quite expensive finance (indeed, this is also a problem with microfinance). An exception is found in multilateral bank lending, although this is quite limited in supply compared to the role played by official lending in the South Korean case. It has also come to be heavily laden with conditionalities that undermine the practice of industrial policy, thereby counteracting the developmental potential of aid, particularly in contexts where trade deficits are admonished. One conclusion that emerges out of this study is that the World Bank and other multilateral lenders should return to this original purpose of providing concessional public finance for industrialization, rather than continuously extending the reach of conditionalities further and further into areas that are outside of their traditional mandate and, in many cases, arguably outside of their expertise (such as governance, which according to recent reports has been quite deplorable within the Bank).

However, a final issue to consider is the fact that the current setting of global imbalances since the early 1980s, led by US imbalances, has been profoundly un-conducive for supporting redistributive transfers from rich to poor countries given that these imbalances encourage resource flows from poor to rich countries (especially to the US). The fact that aid might appear to be somewhat dysfunctional in this context is arguably best understood from this broader perspective, rather than seeking the causes of dysfunctionality in a myriad of behavioural or institutional factors from the side of recipients. The fundamental long-term challenge for instituting a genuinely redistributive aid system concerns the question of how to reverse the pattern of these global imbalances in such a manner that they privilege redistribution to poorer nations, albeit preferably not in a manner that reinforces dependency.

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