ASIAN COUNTRIES AND THE DUTCH DISEASE

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Folha de S. Paulo, April 12, 2010

The Dutch disease does not derive from abundant and cheap natural resources, but from the combination of low wages and a high wage dispersion

The American government was about to declare China an exchange rate-manipulator country, but, since bilateral negotiations continue, the American Treasury decided to postpone the decision, probably because it expects China to yield somewhat, as it did in 2005. In that year the United States Senate voted a 27.5% increase in tariffs on imported goods from China, which did not take place only because in the following years China allowed a 20% appreciation of the renminbi. However, since it once again pegged its currency to the dollar during the crisis, the pressure is back.

The trade deficit between the United States and China is falling since 2008. Even so, eminent economists such as Paul Krugman and Martin Wolf are convinced of the depreciated nature of the renminbi. Wolf lists four arguments presented by those who disagree: “first, while the intervention is huge, the distortion is small; second, the impact on the global balance of payments is modest; third, global imbalances do not matter; and, finally, the problem, albeit real, is being resolved” (*Valor*, April 07, 2010). However, none of those arguments that the *Financial Times* columnist later sought to refute is relevant. The basic fact is simple: China does not have a surplus but rather a trade deficit with the other dynamic Asian countries. Therefore, if the renminbi is artificially undervalued, so are its neighbors' currencies.

What analysts do not understand when they observe the huge current account surpluses of the oil-exporting countries and of the dynamic Asian countries, including China, is that those surpluses derive from those countries' need to neutralize their Dutch disease – that is, to neutralize the chronic overvaluation of their exchange rate. In the case of the Asian countries, the Dutch disease does not derive from abundant and cheap natural resources, but from the combination of low wages and a high wage dispersion between plant engineers and blue-collar workers, as compared to rich countries. Since the exchange rate is determined by the cheaper goods, if the country facing this problem does not manage its exchange rate, it will be determined by those industrial goods (fabrics, for instance), and will preclude the production of sophisticated industrial goods, which require more skilled personnel, pay higher wages, and have a high value-added per capita.

The Dutch disease is a market failure compatible with the long-term equilibrium of a country's current account. This is the reason why a country affected by the Dutch disease, that intends to industrialize and reach increasingly higher levels of industrial sophistication, should necessarily manage its exchange rate in order to shift it from the level of current account equilibrium to the "industrial equilibrium". If the country succeeds in this task (which is not easy), it will necessarily present a current account surplus. This is what happens with the dynamic Asian countries.

From this type of analysis a surprising consequence ensues. As more developing countries become aware of their Dutch disease, they will try to neutralize it and, if they are successful, they will achieve current account surpluses. Therefore, despite the fact that the stock of capital is much higher in rich countries, what we will increasingly see in a near future is developing countries presenting high current account surpluses and making investments in rich countries or lending money to them.