Is social policy now a well-established but ‘new’ form of economic development?

I suggest that much thinking about social policy (debates about the value of spending on areas such as education and health) ignores the ways in which developing countries have been changing since the end of the Cold War: centrally, that on average they tend not to industrialise (focus on manufacturing) but servicise, without a key services sub-sector driving the change. Standard development doctrine has long stressed industrialisation as the general and necessary path to success for developing countries. This view ignores the possibility that services can drive growth in their own right.

My basic idea is that social policy—which is associated with important services sub-sectors (such as education and health) which focus on increasing people’s welfare—is better seen as an expression of servicisation: economies growing in ways that shift economic activity to services, rather than manufacturing, as people and capital leave other sectors, particularly agriculture, where rewards are less.

If structural change in an economy is measured as the sources of shares of Gross Domestic Product (GDP), then these growing ‘factor rewards’ (payments to labour and capital) in the services sectors are caught by the National Income Accounts. Factor rewards in manufacturing are relatively low if there is a process of servicisation. Social policy, therefore, if I am on the right track, is better seen as part of these powerful trends to shift the sites of economic activity to where societies, and sometimes markets, value them more (ie where payments to capital and labour are higher).

This picture is not the common one. It is, however, the global reality in nations such as Vietnam since the end of the Cold War, though it remains under-studied and therefore not well-understood.

Common beliefs are under pressure

Contemporary beliefs about how developing countries change as they grow are under pressure. This pressure, however, is relatively weak compared with that to maintain existing beliefs and norms in relation to industrialisation. My own research interests focus on Vietnam, which has servicised during its post 1992 Economic Miracle, despite donor and Communist Party advocacy of industrialisation. Unusually, Vietnamese policies have shifted to support servicisation, after years following standard international industrialisation doctrine. At the Communist Party level policy shifted around 2018 and at state level early in 2022. There are two related but little discussed facts:

- On average since the end of the Cold War, globally developing countries have servicised—that is the share of economic activities as measured by GDP in services sectors have risen, and the faster they have grown the more they have servicised.
- Whilst donors and scholars discuss industrialisation, servicisation is largely off their 'radar screen'. In Vietnam, GDP/worker in manufacturing has been below the national average, whilst those in services on average are above it. The well-known very high levels of manufactured exports generate relatively very little GDP—perhaps less than 15 percent of gross exports.

Standard development doctrine has long stressed industrialisation as the general and necessary path to success for developing countries. Proposals for capital investments that stress services therefore have little citable research to draw upon. There are almost no mentions of the term 'servicisation' in academic journal abstracts. Standard doctrine tends to see industry as the driver and the rest of the economy, in the main, as needing to support industry. Social spending is therefore seen as a cost to industry, either being consumption (taken from investment), and/or spending on better quality inputs, especially of labour. Workers, it is thought, better support industry if they are healthy and better educated. This view is common, but does not fit with the observable pattern of servicisation where social welfare serving sub-sectors such as education and health are very important contributors to GDP.

Servicisation is generally still off the radar

Work on the Vietnamese Economic Miracle suggests that servicisation, where GDP/worker in services sectors is relatively high (higher than average GDP/worker) is in many ways very different from industrialisation. Developing countries like this are not ones where, as many typically (but not always) think, services are best viewed as a plethora of low-income and backward activities, particularly in urban areas. Rather, it is where rewards to capital and labour are relatively high, so employers and workers move there from other parts of the economy. And, if we look at the data, important services sub-sectors, such as education and health, are part of the story. Their main function is not to support manufacturers, but they drive growth in their own right. In Vietnam, for example, this is clear from the GDP data, which is striking. It is an example of where services sectors are growing relatively fast.

There is much to think about for policy makers and scholars. Much of the discussion is founded on unquestioned assumptions about education and skills—the privileging of white collar work over trades, the belief in industrialisation and so the need to produce suitable skills for an imagined reality. In fact, it is clear that industrialisation is not driving growth, on average. There is formidable bias: a 2018 World Bank report on Vietnam clearly believed that white-collar skills were far more important than trades. The common belief is that trades skills are there to serve industrialisation, focussing on industrial workers. Arguably, the notion of trades skills as inputs to industrialisation platforms on elite beliefs rather than underlying economic fundamentals, given servicisation. However, the GDP data shows that higher payments to capital and labour occur in services. Perhaps this is, economically, to do with contestations over positionality and power: GDP data reports actual payments to labour and capital, and it is not clear that these reflect higher productivity.

If the standard economic conception of economic growth is through the accumulation of capital as well as using it more efficiently, such as increasing labour productivity, then a services-focus seems likely to be different. Services tend often to use little fixed capital and it is not clear what drives the increases in GDP/worker. Services do not generally look like factories – they do not usually turn physical things into other physical things—this is unlike industry, where fixed capital takes the form of machines, and outputs are easily priced and relatively homogenous commodities.

As there is almost no academic research on servicisation, it has not been properly explored. Common understandings of issues such as spending on social welfare and other social policies are not well informed by thought-through and well researched studies. This suggests that what are called social welfare issues are likely different from how they are generally understood.

Such labels should be examined for what they obscure: social welfare is, possibly, better understood as an attempt to grapple with patterns of economic growth—servicisation—that are frequently dismissed as 'premature deindustrialisation', rather than expressing societal and economic pressures to shift labour and capital to areas of activity that include those labelled as 'social welfare', but are in fact generating higher contributions to GDP than manufacturing.

What is social policy up to?

So, perhaps what we are seeing in Southeast Asian 'welfare regimes' since the end of the Cold War is a reconfiguration to take account of servicisation, but where the empirical picture is confused because this goes against widely accepted beliefs. Part of this is increased focus on services sub-sectors that have traditionally been labelled as a social cost, or perhaps an investment in labour, justified by the hope for faster industrialisation, comparable to investment in certain types of infrastructure. That would perhaps have implications for changes on the supply side—how the outputs of social policy are delivered.

My conclusion is that there are great possibilities for research to contribute to a better understanding of the nature of social welfare in servicising economies. Rather than seeing them as a cost to growth, it is better to see them as the sites of major contributions to economic development as payments to labour and capital in them are relatively high.

Political scientist Andrew Macintyre concluded that one way of discussing variations in historical change patterns in East Asia is to frame them in terms of the relevance or irrelevance of policy. His broad conjecture was that policy was far less important to the writing of plausible histories of change in Southeast Asia than in Northeast Asia. I note Chinese research arguing, in a context where the Chinese economy started to shift to services strongly in the early 2010, that, in effect, Chinese policy makers do not, and have not, coherent thought-through servicisation strategies. By contrast, as I have already mentioned, Vietnamese Party strategy, and then State policy, appears to have grown out of both concrete reality and a need to cope with the failure to industrialise, despite donor and Party support for it. There is debate in India about whether services can or cannot offer a reliable platform for economic growth.

Part of this extremely broad question relates to the following:

First, the extent to which resources are subject to the influence, if not control, of state power. If so, are they deployed to seek to drive sector strategy ('industrialisation') but, historically, have been diverted by the political economy to places (such as services) where factor rewards are higher? This seems to have been the case in Vietnam where official corruption has been so high as to be interpretable as a form of property. If so, officials had strong incentives to respond, not to strategy but to perceived material advantage. Getting at such unknowns requires powerful research assets, knowledge of local institutions 'as they really are', and a collegiality that does not suffocate iconoclasm. Note that Vietnamese are already publishing studies of their own economy that refer to the 'shift to services' as well as the nature and scope of corruption.

Second, managing the conceptual tangle that follows from what the GDP data shows, which is the lack, within services, of a 'leading sector' comparable to manufacturing within industry. This has important implications for the basic 'vision' of mainstream microeconomics about manufacturing, for standard microeconomic theory presents a model of a single product firm that is clearly inspired by (and relies upon) belief in applying to the general issue of how to understand economic activity ideas of factories that turn 'stuff into stuff', offering support for the technical device of a production function. This vision does not easily fit with many services activities such as education and health. Further, no services sub-sector, according to the GDP data for developing countries like Vietnam, generates relatively high levels of payments to labour and capital and plausibly (like manufacturing in historical experiences such as post-war Japan) 'drives growth'. Within services, though real estate and financial services generate relatively high rewards to labour and capital, it would seem a big ask to argue that (with exceptions such as Singapore and Hong Kong) these are conceptually capable of acting as a trope, like manufacturing. Notably, such tropes underpin the idea that classification of broad sectors of the economy ('industry', 'services' etc) should be based on similarities in their technologies: a power plant may thus be grouped with a shirt-factory under 'industry', but is it so wise to group such services sub-sectors as tourism, financial services and education together on such grounds? In many ways, 'services' is, in fact, a residual category—neither 'industry' nor agriculture (or forestry and fishing). This is a further indication that 'servicisation' is neither well thought-through nor well researched.

It is therefore likely that considered research on servicisation in East Asia, especially Southeast Asia, will, eventually, give us an understanding of how services sub-sectors interact, without one being a leading sub-sector: for example, through synergies of managerial, entrepreneurial, and work skills. We will then be able to see how areas currently viewed through the lens of social welfare fit into stories and analyses of dynamic social and economic change. Macintyre's point may still stand, as the general lack of servicisation strategies and analyses has meant that ‘growth has happened’, rather than ‘being caused to happen’, and that in Southeast Asia such change processes have long histories. It is therefore unwise to view social welfare issues, perhaps since the end of the Cold War, through lenses of ‘late industrialisers’ or ‘premature de-industrialisers’.

Two conclusions stand out:

- First, that there has been a major problem in mainstream analysis and policy recommendations. Whilst the natural response is to ignore this and develop new analyses that focus on servicisation (and there are signs of this already), the serious scholarly task is to explore the methodological implications and the standards applied to mainstream research by consumers of it. Large amounts of tax-payer money financed (and probably still do) studies and policy recommendations that were and remain wrong.
- Second, building on these methodological problems, serious attention should be paid to analyses of change in developing countries that explain and evaluate servicisation. Servicisation is not only deployed by rapidly growing countries such as Vietnam, but also seems to happen in countries facing major social and political tensions, where, it is likely, it cushions populations facing major challenges.

Should taxpayer-funded policy advice treat an increasing share of services in GDP as a failure and aid resources seek to support manufacturing? To train welders rather than adapt information technology for small local services companies? To lend for infrastructure to support manufactures exports rather than services?

Image: A teacher and student at a primary school in Vietnam. Credit: ILO Asia Pacific/Flickr.