Middle-Income Trap - should companies be worried?

An exploratory study of the potential impact by Middle-Income Trap on Sweden-related companies in Thailand

ELIZABETH MERKOULOVA & ELIN KARLSSON NYCANDER

The term *Middle-Income Trap* (MIT) is relatively new, originating thirteen years ago, but has since generated significant debate. It is used by politicians to channel national reforms and has given rise to a vast amount of research about growth slowdowns in *middle-income countries* (MICs). The term describes the higher prevalence of *economic growth slowdowns* in MICs, which impedes their transition into high-income countries. Three quarters of the world lives today in MICs, many of which are dependent on the presence of foreign firms for continued growth and development. This master thesis has therefore explored the phenomenon from a new perspective - studying its effects on international companies.

The MIT phenomenon was first described by Garrett in 2004, who argued that MICs are not able to compete with neither the low-income countries *low-wage economy* nor the high-income countries *knowledge-economy*. The term MIT was first defined by Gill & Kharas. The world bank published their research in 2007 and initiated an ongoing debate regarding the existence of the phenomenon. As of today, there are plenty of studies proving or disproving the existence of the MIT, and yet the term has no universally accepted definition.

Eichengreen, Park & Shin (2013) tried to understand under *which* circumstances countries experience economic growth slowdowns and identified five national factors that correlate positively with economic stagnation: *Human capital, Political regime changes, External factors, Technology content of export* and *Financial instability*. These factors were used to capture the characteristics specific to a country affected by the MIT.

Furthermore, to explore MIT from the perspective of international companies, the act of internationalisation has been crucial to examine. The global market of today has made the internationalisation of companies a common move. Depending on the nature of the company and their home market, the motives for the business to become international can differ. The framework by

Yip is fitting to understand these different motives by dividing them into four categories called drivers; market, government, competitive and cost (Johnson et al. 2017). In this study, we have utilized this framework to explore the motives behind establishment in a foreign country.

The phenomenon was decomposed into five different factors that according to Eichengreen, Park and Shin (2013) have a correlation to growth slowdowns, combined with Yip's framework and then explored through interviews with Sweden-related companies active in Thailand. Thailand is a middle-income country that recently experienced economic stagnation. It was found that even though all the five factors had an effect on companies, there was one MIT aspect that affected almost all companies regardless of their internalisation strategy: *Human capital*. More specifically, companies were affected by lack of certain competencies in the labour market. Many companies struggled to find good engineering skills, leadership skills and the combination of English knowledge and a specific skill. Today, this problem is solvable through higher salaries and by providing educations for employees. However, this issue could eventually lead to more serious consequences as it impedes the transition into a *technologically advanced economy*. It was concluded that MIT creates a peculiar labour market with effects reaching most companies, regardless of their field of work or strategy.

References

Eichengreen, B., Park, D. & Shin, K. (2013). Growth slowdowns redux, National Bureau of Economic Research. Available online: https://www.nber.org/papers/w18673.pdf [Accessed: 22 October 2019]

Johnson, G., Whittington, R., Regner, P., Scholes, K. and Angwin, D. (2017). Exploring Strategy, 11th edn. Harlow: Pearson