

## The development imperative

In late 2004, a very powerful earthquake set off a series of tsunamis which devastated many countries in SE Asia and eastern Africa. Hundreds of thousands died and tens of thousands went missing.

You might be wondering, why are we talking about an earthquake. What does this have to do with development? Economic progress does not bring with it the ability to reduce the occurrence of these natural disasters, but it does create the capacity to reduce the human devastation. Many of those who suffered the greatest devastation lived in low-lying areas prone to flooding on marginal land in low-quality housing.

Economic development is in fact about life-and-death.

Undernourishment and malnutrition affect large segments of the global population; of those who suffer, they disproportionately live in developing nations. While over the last several decades great strides have been made, particularly in reducing the percent of the population who experiences food insecurity, it remains a serious problem and when combined with preventable diseases accounts for an overwhelming share of the millions of children under the age of five who die every year in developing countries.

Hunger and disease is a vicious circle! In the time that you have spent listening to this lecture so far, several children will have perished unnecessarily.

Clean drinking water, basic toilets, and good hygiene are critical for the survival and development of children.

Yet in 2020, 2.4 billion people do not have access to improved sanitation and 663 million do not have access to improved water sources. Access to water, sanitation, and hygiene is even more important with coronavirus crisis. Children remain particularly vulnerable.

We are confronted with a monumental challenge. Confronting these problems requires institutional change. Identifying the social structures- particularly the political-economic structures which serve to preserve extreme poverty and privation.

## Poverty in less-developed world (1)

According to a former World Bank president, the “absolute poor,” human beings who suffer “a condition of life so degraded by disease, illiteracy, malnutrition, and squalor as to deny its victims basic human necessities.... [It] is life at the very margin of physical existence.” For most of us, I imagine, this condition is beyond comprehension as it is for most citizens of developed countries.

Undoubtedly, poverty is one of the most pressing problems confronting the world today. According to the World Bank, 2/3rd of the world’s population lives on less than 10 dollars per day and 1/10<sup>th</sup> on less than 1.90 dollars, which is the line for extreme poverty set in 2015.

This figure shows apposite trend, specifically that the proportion of the global population which lives in extreme poverty has been declining over the last four decades.

## Poverty in less-developed world (2)

While the proportion of the population which lives in extreme poverty has been declining, when we look at the regional distribution of people living in extreme poverty, it becomes apparent that these improvements have not been benefitted everyone equally. There have been great improvements in the headcount—the numbers of poor falling below the extreme poverty line— across parts of Asia; however Sub-Saharan Africa has not fared so well. There is a severe limitation of this and the previous measure— both measures are completely insensitive to the severity of the poverty.

## Poverty in less-developed world (4)

This interactive graphic introduces to us an alternative perspective on measuring poverty: the poverty gap. The poverty gap does a better job capturing the severity of poverty as it informs us of the amount of income necessary to lift everyone out of extreme poverty. This graphic plots the poverty gap against the poverty headcount rate. It shows us the share of the population living in extreme poverty as well as how far below that poverty line they are.

Poverty is a complex problem and while an income transfer suffices as a short-run solution to the most extreme suffering, a long-run solution which permanently eradicates poverty requires the creation of jobs that pay above poverty wages.

If we were to look at the poverty gap relative to income, you would see that in the less-developed world the poverty gap is modest relative to income. This suggests that poverty is a problem not just of income, but also of distribution. It is not an inability to produce—it is not a technical matter— that creates poverty; rather, poverty results from political-economic power structures.

## Millennium development goals

In late 2000 the United nations adopted the millennium development goals. Follow the link below and spend a few minutes reading over the report on the Millennium development goals which can be obtained by clicking the button below.

You will see that much progress has ben made; yet there also remains much more to be done if we are to eradicate poverty and privation.

While most of the focus has been on income, which is an important indicator of a nation's economic progress, we will see in later lectures that there are many other insightful methods as well.

## The development enigma

Sometime after WW2, Development economics emerged as a subfield which focused on the problems of the so called "third world." This field sought to answer, and for the most continues to seek answers to, questions such as:

-why are some countries rich and others poor?

-why is there so much human suffering in so many countries?

-why is Africa less developed than Latin America?

-How have countries in East Asia, and I am thinking specifically Taiwan and South Korea, achieved economic success?

-Why has India with so many highly educated citizens not been able to follow the same path South Korea took in transitioning to higher and more equitable economic development?

-How has China, with its immense population, surpassed India in per capita income? In the late 1980's these two countries had roughly the same per capita income; however, now china has per capita income nearly five times higher than India.

These important questions have no easy answer. However, what we can do is look to the historical experiences of different countries, both those who have been successful and those who have failed and start to identify patterns and regularities. At the very foundation of development resides a moral dimension- a belief that all people deserve the opportunity to realize certain fundamental values.

Here you can see a list which is not meant to be all-inclusive:

Before turning to the recent trends, let me conclude by stating that while development did not emerge as distinct field until the 20<sup>th</sup> century, one can find similar lines inquiry throughout the history of economic thought. Consider the title of perhaps the most oft-cited and least read texts in economics- Adam Smith's *Inquiry into the Nature and Causes of the Wealth of Nations*.

## Recent trends in economic growth

Let's talk about growth in the US for a moment. For approximately the last 5 decades real wages in the US have been stagnant. Moreover, a significant part of the permanent workforce has been replaced by a contingent workforce. This is a troubling trend because a contingent workforce has fewer rights, lower incomes, and increasingly precarious future. Moreover, the extent of inequality in the US is at levels unseen for almost a century. In the 21<sup>st</sup> century, the rich have been seizing an increasing share of all the wealth being created while the poor continue to get poorer. The point we should take from this discussion of the US is that even developed economies can experience significant problems achieving long-run economic progress.

Undoubtedly, the problems are worse in the developing countries. The range of living standards that one encounters in the developing world is staggering. This is something I have witnessed firsthand when I disembarked from the plane in Cochabamba, Bolivia. The indignance I observed was beyond anything I could have comprehended before. This was an extremely influential time in my life as I immediately started to question how such extreme's could exist- extreme's both between and within nations.

Economics is the framework with which we can find the most insightful answers to the most pressing questions confronting society.

This interactive graphic shows how average income has evolved in different countries over time. The data visualized here is insightful for seeing disparities in living standards across countries: that is for comparative purposes.

## Low- and middle-income nations

In this course we will mostly be concerned with the low- and middle-income countries which constitute about 62% of all nations. The world bank has 4 classifications:

- Low-income countries have gross national income per capita less than \$1,035
- Lower middle-income countries have gross national income per capita between \$1,035 and \$4,045
- Upper middle-income countries have gross national income per capita between \$4,045 and \$12,536
- High-income countries have gross national income per capita of more than \$12,536

This table shows how the world bank classifies each country. The interactive graphic on the next slide allows you to see how each countries classification has changed over time.

## Why development and why now

The rich western nations did not become so overnight. In fact, countries like Great Britain, the United States, as well as many other western European nations reached this status through a very long, slow, and uneven process, centuries in fact.

The countries that we consider less-developed have had a much shorter time to develop as independent political entities than their richer counterparts. The time dimension is critical, as is the fact that many less-developed nations did not escape the shackles of colonization until after WW2 when the United Nations began to apply pressure to decolonize. Post-colonial construction entails two simultaneous goals: nation building and economic and social development.

The patterns of production, class, and power that exist in less-developed nations were inherited from the past. This adverse path dependence undoubtedly exists as an important barrier to social and economic development.

## Economic growth and development require structural change

Originating from Robbins highly influential 1932 Essay on the Nature and Significance of Economic Science, economics is often defined as how societies can best allocate scarce resources among competing uses. This framework postulates marginal adjustments independent of historical time until a maximum has been found by an individual decision maker. It is assumed that this reactive behavior by the decision-making agent occurs within an exogenously determined institutional setting. Notice that I referred to the behavior as reactive. The preferences of the decision maker are assumed to be fixed as are the resources; as a result of these assumptions, the decision maker simply responds to externally determined stimuli- they have no agency.

A successful development process is a dynamic process; a process that requires new institutional patterns and organizational structures. The less developed the nation, the greater the structural change that must be undertaken.

Here you can see the 5 major structural changes agreed upon by most development economists and economic historians:

1. Growth and development are strongly associated with increasing the share of output from industrial activities. Relative to agriculture, industry tends to be more technologically intensive, thus wages and productivity tend to be higher.
2. Paralleling the first change is a decrease in the share of output from agriculture.
3. The developing nation needs to transcend the colonial legacy of being a primary exporter- an exporter of agricultural and fishing products, forestry products, extractive minerals, etc...
4. Becoming more productive and transitioning away from primary exports into secondary and tertiary exports (and by this, I mean manufactured goods and services) requires an increased application of human capital and knowledge. This is a synergistic process which is a consequence of an expanded application of physical capital.
5. These structural changes represent essential institutional change. Institutional change refers to a change in the organizational rules that govern social interactions. Many of these rules are determined and enforced by the state. Thus, the state has an important role in creating the environment in which progressive change can occur.

## Barriers to development

The first step of institutional change requires identifying the problematic institutions: what are the barriers to development. Here you can see some examples of both internal and external barriers. Each country will face a unique set of challenges that change over time. Not surprisingly, the greater the obstacles a country, whether they internal or external, the slower the progress. The challenge is identify how successful countries have overcome successive barriers and try to learn from their experiences.