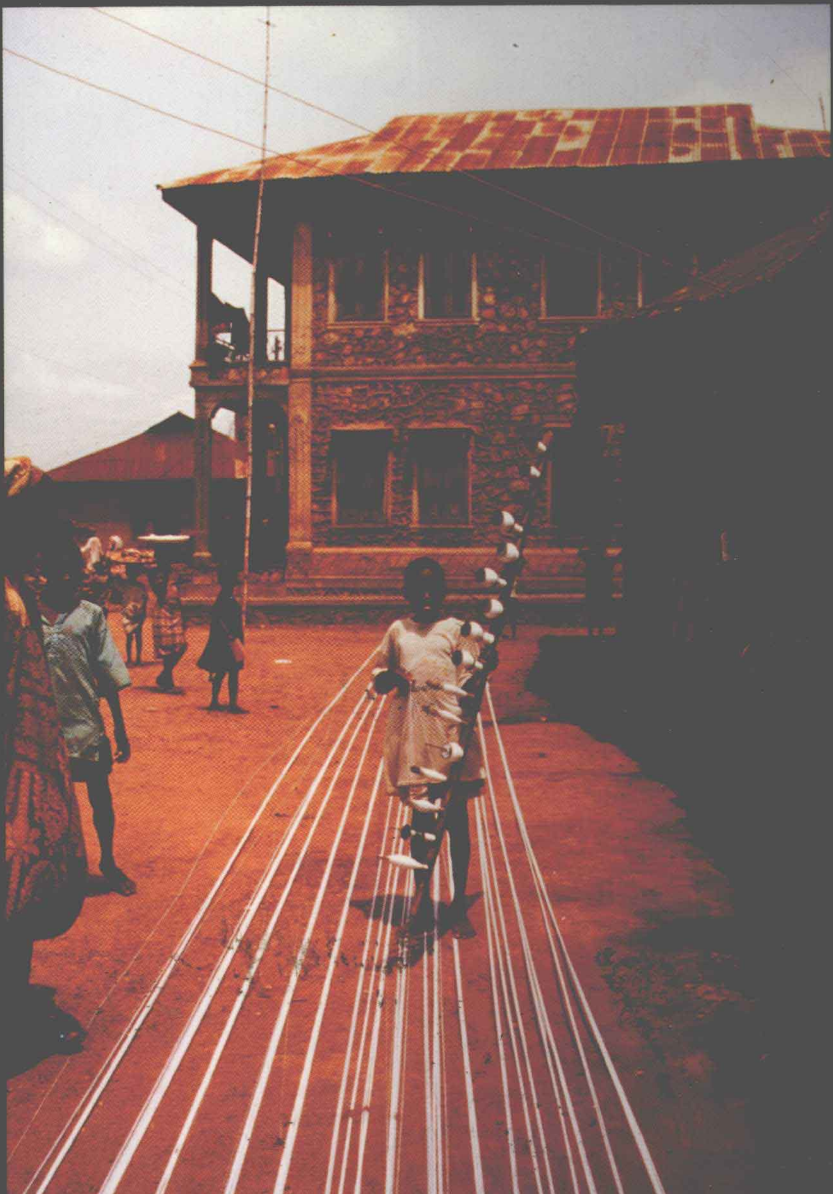
Leading Issues in Economic Development

SEVENTH EDITION

Gerald M. Meier
James E. Rauch



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University of California, San Diego

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To the next generation of development economists.

–G.M.M.

To my mother and to the memory of my father.

–J.E.R.

PREFACE

The economics of development is one of the most exciting subjects in social science. Why, two centuries after the Industrial Revolution, are poverty and its attendant ills so prevalent in most of the world? And what can be done about it? Nobel Prize–winning economist Robert Lucas wrote of the questions addressed by development economics, "Once one starts to think about them, it is hard to think about anything else" ["On the Mechanics of Economic Development," *Journal of Monetary Economics* 22 (July 1988), p. 5].

Development economics is also a very frustrating subject. Unlike most areas within economics, there exists no consensus on what the student should know. Two scholars can with equal justification write two completely different textbooks.

The aim of this book is to convey as much of the excitement of development economics and as little of the frustration as possible. To this end we have avoided writing the ordinary type of textbook, instead culling the most insightful readings from the diffuse field of development and bringing them into conceptual order. By using this distinctive approach we allow for a variety of perspectives while keeping in sight the most important overarching themes. The section "Using This Book" (p. xix) describes our strategy of combining excerpted readings ("Selections") with our own "Overviews," "Notes," "Comments," and "Exhibits."

After being responsible for the previous six editions of *Leading Issues in Economic Development* over the past 35 years, Professor Meier has now selected Professor Rauch to upgrade and modernize this seventh edition and to perpetuate subsequent editions. This edition is mainly Professor Rauch's effort. It reflects his desire to strengthen the analytical and quantitative dimensions of development economics and to illuminate contemporary—and future—problems of development policymaking. In all, it provides fresh and serious attention to the interplay between development experience, changing views of economists, and policy.

While this seventh edition maintains the format of previous editions, the inclusion of a new author has brought many changes relative to the sixth edition:

- New chapters on income distribution and on development and the environment have been added while other chapters have been consolidated.
- Most of the Selections and Notes are new.
- The representation in the Selections of articles from leading professional journals has increased.
- The Selections make greater use of statistical analysis, and an Appendix, "How to Read a Regression Table," has been added to ensure that these Selections are easily accessible to all readers.

We wish to express our appreciation to the authors and publishers who have granted permission to use excerpts from publications for which copyrights exist. Specific acknowledgment is given with each Selection. Some parts of the original versions of the excerpted materials have been omitted out of consideration for relevance and to avoid repetition. In some instances, tables and diagrams have been renumbered and the footnotes have been deleted or renumbered.

We would like to thank a number of extremely busy people who generously took time out to provide advice or to comment on portions of the manuscript: Richard Carson, Graham Elliott, Peter Evans, and Dani Rodrik. We would also like to acknowledge the valuable research assistance of Neville Francis, Timothy Kane, Paula Lindsay, and Donald McCubbin. James Rauch wishes to thank his wife, Doris

Bittar, for making room in her life for this book during its final months of preparation. Kenneth MacLeod has been a very helpful and patient editor. Finally, we are grateful to the entire profession of social scientists whose writings on development provide the foundation for this volume.

USING THIS BOOK

Instructors and students can use this book more like a main text or more like a supplementary reader. To facilitate the latter approach the contents have been designed to allow individual freedom of choice in deciding what chapters and Selections to read and in what sequence. If the former approach is taken, the organizational and thematic guidance of the chapter Overviews can be followed and the chapters can be read in numerical order.

The chapters include the following materials:

Overviews: These are introductory essays that show how the subsequent chapter materials fit together and elucidate one or more overarching themes. They sometimes contain ideas that are not explicitly presented by the other chapter materials.

Selections: These are the core of the book. They present a broad sample of the major contributions by scholars and practitioners on the central issues in economic development. Each Selection has been edited for the sake of brevity and to highlight the points of greatest relevance for the chapter in which it appears.

Notes: These serve two purposes. One is to expound important ideas that are extant in the literature but are not presented as clearly or simply as we would like. The other is to present more original material that complements the Selections.

Comments: Like the Notes, these serve two purposes. One is to clarify or expand upon the immediately preceding Selection. The other is to suggest additional readings on the subject of the immediately preceding Selection.

Exhibits: These are tables and charts that provide empirical illustrations and data on topics under discussion.

Starting with Selection III.1, some Selections include regression tables. Readers without econometric training are urged to refer to the Appendix to get the most insight from these Selections.

CONTENTS

EXHIBITS

CHAPTER I

Introduction

Overview

The subject of this book is the economics of less developed countries, sometimes called "developing countries." Yet we must admit from the start that there is no universally accepted definition of "less developed country" (LDC). Roughly speaking, the definition in use by the writers whose work is excerpted in this book is the countries of Latin America, North Africa and the Middle East, sub-Saharan Africa, and Asia minus Japan and the countries that were formerly members of the Soviet Union: in short, what used to be called the Third World. When the border that separated East and West Germany became obsolete, so did the boundaries that separated the classification "Second World" from the classifications "First World" and "Third World." Yet the countries of Eastern Europe and the former Soviet Union, no matter how poor, are currently labeled "transition" countries rather than "less developed" countries, and are the subject of "transition economics" rather than "development economics." Moreover, a number of formerly Third World countries such as Israel, Singapore, and Taiwan would appear to have graduated to "more developed" or "industrialized" status.

Given this current state of flux regarding country classifications, it seems more important than ever to be careful about how to measure a country's level of "development." The Note that begins the first section below starts with the measure by which countries are ordered in Exhibit I.A.1 (and in many other Exhibits in this book): per capita GNP in U.S. dollars. As described in the Note, because of evidence that the purchasing power of U.S. dollars is greater in poor than in rich countries, per capita GNP in U.S. dollars is increasingly being replaced by the second measure in Exhibit I.A.1, per capita GNP in "international dollars." Exhibit I.A.2 shows that this "correction" of exchange-rate converted per capita income tends to be greater, the poorer the country relative to the United States. Selection I.A.1 by Jagdish Bhagwati and the following Comment attempt to explain why services are so much cheaper relative to commodities in poor countries than in rich countries, cheaper services being the chief reason the purchasing power of the dollar is greater in poor countries. Exhibit I.A.1 also contains an indicator of poverty that is used to supplement (or replace) per capita income as a measure of development. The development of an internationally comparable poverty line is discussed in the selection by the World Bank, I.A.2. The last two columns of Exhibit I.A.1, life expectancy and adult illiteracy, are used as inputs to the Human Development Index (HDI), the last measure of development discussed in Note I.A.1. Exhibit I.A.3 shows exactly how the HDI is computed, Exhibit I.A.4 shows that countries can have very similar per capita incomes yet quite different HDI values, and Exhibit I.A.5 ranks countries from highest to lowest HDI values. The HDI owes much to the work of Amartya Sen, which is the subject of the Comment following Exhibit I.A.5.

The first section concludes with Exhibit I.A.6, which shows two important systematic differences between low- and high-income countries that are not included in any of the measures of development discussed in the Note. First, population growth is higher in low-income countries. The (unweighted) average annual growth rate of population for the low-income economies in Exhibit I.A.6 was 2.6 percent in the period 1980–90 and 2.3 percent in the period 1990–95, compared with 1.0 percent and 0.8 percent respectively, for the high-income economies. The cause of more rapid population growth in low-income countries is easily traced to an incomplete "demographic transition" from high birth rates and death rates to low birth rates and death rates. The (unweighted) average birth rates for the low- and high-income economies in 1995 were 38 births per thousand persons and 13 births per thousand persons, respectively. (All figures reported in this paragraph and the next not computed from Exhibit I.A.6 were computed from the 1997 *World Development Indicators* CD-ROM.) The (unweighted) average death rates for the low- and high-income economies in 1995 were 13 deaths per thousand persons and 8 deaths per thousand persons, respectively. Thus population growth is more rapid in low-income countries because death rates have dropped to near the level of high-income countries but birth rates have not. A key factor in bringing down death rates in low-income countries was control of major infectious diseases. This control was fostered by international aid agencies and its success did not require high incomes in the recipient countries. One consequence of the much higher birth rates in low-income countries is that their populations tend to be much younger than in high-income countries. The (unweighted) average share of the population less than 15 years old was 43 percent in the low-income economies in 1995 compared with 21 percent in the high-income economies.