

Contents

Preface

xv

International Development Resources on the Internet

xxiii

PART ONE

Development and Growth

1

Patterns of Development

3

Three Vignettes 3 | *Malaysia* 3 | *Ethiopia* 5 | *Ukraine* 6 | *Development and Globalization* 8 | Rich and Poor Countries 10 | Growth and Development 13 | *Diversity in Development Achievements* 15 | Approaches to Development 16 | *The Study of Development Economics* 18 | Organization 19 | Summary 20

2

Measuring Economic Growth and Development

23

Measuring Economic Growth 24 | *Measuring GDP: What Is Left Out?* 25 | *Exchange-Rate Conversion Problems* 27 | Economic Growth around the World: A Brief Overview 32 | JARED DIAMOND: GUNS, GERMS, AND STEEL 34 | *Economic Growth, 1970–2010* 36 | What Do We Mean by *Economic Development?* 38 | *Measuring Economic Development* 40 | HUMAN DEVELOPMENT DEFINED 41 | WHY USE LOGARITHMS? 43 | *What Can We Learn from the Human Development Index?* 44 | *Millennium Development Goals* 46 | TARGETS OF THE MILLENNIUM DEVELOPMENT GOALS 47 | Is Economic Growth Desirable? 50 | Summary 53

3

Economic Growth: Concepts and Patterns

55

Divergent Patterns of Economic Growth since 1960 56 | BOTSWANA'S REMARKABLE ECONOMIC DEVELOPMENT 59 | Factor Accumulation, Productivity, and Economic Growth 60 | CALCULATING FUTURE VALUES, GROWTH RATES, AND DOUBLING TIMES 61 | Saving, Investment, and Capital Accumulation 64 | Sources of Growth Analysis 66 | Characteristics of Rapidly Growing Countries 74 | 1. *Macroeconomic and Political Stability* 75 | 2. *Investment in Health and Education* 77 | 3. *Effective Governance and Institutions* 79 |

4

Theories of Economic Growth

89

The Basic Growth Model 91 | The Harrod-Domar Growth Model 94 | *The Fixed-Coefficient Production Function* 94 | *The Capital-Output Ratio and the Harrod-Domar Framework* 96 | *Strengths and Weaknesses of the Harrod-Domar Framework* 98 | ECONOMIC GROWTH IN THAILAND 101 | The Solow (Neoclassical) Growth Model 103 | *The Neoclassical Production Function* 103 | *The Basic Equations of the Solow Model* 104 | *The Solow Diagram* 108 | *Changes in the Saving Rate and Population Growth Rate in the Solow Model* 109 | POPULATION GROWTH AND ECONOMIC GROWTH 112 | *Technological Change in the Solow Model* 113 | *Strengths and Weaknesses of the Solow Framework* 116 | Diminishing Returns and the Production Function 117 | EXPLAINING DIFFERENCES IN GROWTH RATES 118 | *The Convergence Debate* 121 | Beyond Solow: New Approaches to Growth 125 | Summary 127

5

States and Markets

129

Development Thinking after World War II 130 | MARKET FAILURE 133 | Fundamental Changes in the 1970s and 1980s 137 | GHANA AFTER INDEPENDENCE 139 | THE DECLINING EFFECTIVENESS OF GOVERNMENT INTERVENTION IN THE MARKET: KOREA, 1960S-2010 143 | Structural Adjustment, the Washington Consensus, and the End of the Soviet Model 144 | *Soviet Command Model to Market Economies: The Great Transition* 148 | *Was the Washington Consensus a Success or Failure?* 153 | Summary 159

PART TWO

Distribution and Human Resources

6

Inequality and Poverty

165

Measuring Inequality 166 | Patterns of Inequality 172 | *Growth and Inequality* 174 | *What Else Might Cause Inequality?* 177 | Why Inequality Matters 178 | Measuring Poverty 180 | *Poverty Lines* 181 | NATIONAL POVERTY LINES IN BANGLADESH, MEXICO, AND THE UNITED STATES 183 | *Why \$1.25 a Day?* 186 | *Dissenting Opinions on the Extent of Absolute Poverty* 191 | WHO IS NOT POOR? 192 | *Poverty Today* 192 | *Who Are the Poor?* 193 | *Living in Poverty* 195 | Strategies to Reduce Poverty 197 | *Growth is Good for the Poor* 198 | *Sometimes Growth May Not Be Enough* 200 | *Pro-Poor Growth* 201 |

7

Population

217

A Brief History of World Population 218 | *The Demographic Transition* 220 | *The Demographic Situation Today* 224 | TOTAL FERTILITY RATES 225 | *The Demographic Future* 227 | POPULATION MOMENTUM 229 | The Causes of Population Growth 231 | *Thomas Malthus, Population Pessimist* 232 | *Why Birth Rates Decline* 233 | Population Growth and Economic Development 236 | *Population and Accumulation* 237 | POPULATION GROWTH, AGE STRUCTURE, AND DEPENDENCY RATIOS 239 | *Population and Productivity* 241 | *Population and Market Failures* 243 | Population Policy 245 | *Family Planning* 246 | *Authoritarian Approaches* 249 | MISSING GIRLS, MISSING WOMEN 251 | Population Issues for the Twenty-First Century 253 | Summary 254

8

Education

257

Trends and Patterns 258 | *Stocks and Flows* 259 | *Boys versus Girls* 263 | *Schooling versus Education* 264 | Education as an Investment 267 | *The Rate of Return to Schooling* 269 | *Estimated Rates of Return* 272 | *First-Generation Estimates* 273 | ESTIMATING RATES OF RETURN FROM WAGE EQUATIONS 275 | *Second-Generation Estimates* 276 | *Puzzles* 278 | RETURNS TO SCHOOLING AND INCOME OPPORTUNITIES 279 | *Making Schooling More Productive* 281 | *Underinvestment* 282 | *Misallocation* 282 | *Improving Schools* 286 | *Reducing the Costs of Going to School* 287 | MEXICO'S PROGRESA 288 | *Inefficient Use of Resources* 290 | *It Is about More than the Money* 293 | COMBATING TEACHER ABSENCE 294 | Summary 298

9

Health

299

What Is Health? 302 | LIFE EXPECTANCY 305 | *Transitions in Global Health* 307 | *The Epidemiologic Transition* 308 | The Determinants of Improved Health 310 | Health, Income, and Growth 313 | *Income and Health* 314 | HOW BENEFICENT IS THE MARKET? A LOOK AT THE MODERN HISTORY OF MORTALITY 318 | *Health and Productivity* 319 | *Health and Investment* 320 | Three Critical Diseases 321 | MALARIA, YELLOW FEVER, AND THE PANAMA CANAL 322 | *HIV/AIDS* 323 | HIV/AIDS, MALARIA, AND TUBERCULOSIS: SOME BASICS 324 | *Malaria* 329 | MAKING MARKETS FOR VACCINES 330 | *Tuberculosis* 333 | What Works? Some Successes in Global Health 335 | *Preventing HIV/AIDS in Thailand* 336 | *Controlling Tuberculosis in China* 336 | *Eradicating Smallpox* 337 | *Eliminating Polio in Latin America* 338 | *Preventing Deaths from Diarrheal Disease* 340 | *Lessons Learned* 342 | Health Challenges 343 | Summary 344

PART THREE

Macroeconomic Policies for Development

10

Investment and Savings

349

Using Investment Productively: Cost-Benefit Analysis 351 | *Present Value* 351 | *Opportunity Costs* 355 | *Shadow Prices* 355 | *Welfare Weights* 356 | Barriers to Productive Public and Private Investment 357 | Barriers to Doing Business 359 | Foreign Direct Investment 363 | *FDI Patterns and Products* 364 | *Benefits and Drawbacks of FDI* 365 | *FDI and Growth* 369 | *Policies Toward Foreign Direct Investment* 370 | Savings 374 | Household Saving and Consumption 376 | Corporate Saving 379 | Government Saving 380 | Foreign Saving 384 | Summary 388

11

Fiscal Policy

391

Government Expenditures 393 | *Categories of Government Expenditures* 394 | REINING IN FISCAL DECENTRALIZATION IN BRAZIL AND CHINA 398 | *Government Revenue and Taxes* 399 | TAX RATES AND SMUGGLING: COLOMBIA 401 | *Taxes on International Trade* 401 | *Sales and Excise Taxes* 402 | *Personal and Corporate Income Taxes* 404 | *New Sources of Tax Revenues* 404 | *Changes in Tax Administration* 405 | *Fundamental Tax Reform* 405 | TAX ADMINISTRATION IN INDIA AND BOLIVIA IN THE 1980S 406 | INDONESIAN TAX REFORM 407 | Taxes and Income Distribution 411 | *Personal Income Taxes* 412 | *Taxes on Luxury Consumption* 413 | *Corporate Income and Property Taxes: The Incidence Problem* 414 | Economic Efficiency and the Budget 417 | *Sources of Inefficiency* 417 | *Neutrality and Efficiency: Lessons from Experience* 418 | Summary 420

12

Financial Development and Inflation

421

The Functions of a Financial System 423 | *Money and the Money Supply* 423 | *Financial Intermediation* 426 | *Transformation and Distribution of Risk* 426 | *Stabilization* 427 | Inflation 427 | *Inflation Episodes* 428 | HYPERINFLATION IN PERU, 1988–90 431 | Monetary Policy and Price Stability 432 | *Monetary Policy and Exchange-Rate Regimes* 433 | *Sources of Inflation* 435 | *Controlling Inflation through Monetary Policy* 438 | *Reserve Requirements* 439 | *Credit Ceilings* 439 | *Interest-Rate Regulation and Moral Suasion* 440 | *International Debt and Combating Recessions* 441 | Financial Development 442 | *Shallow Finance and Deep Finance* 443 | *Shallow Financial Strategy* 444 | *Deep Financial Strategy* 447 | *Informal Credit Markets and Micro Credit* 449 | DOES MICRO CREDIT REDUCE POVERTY? 451 | Summary 453

13

Foreign Debt and Financial Crises

455

Advantages and Disadvantages of Foreign Borrowing 458 | Debt Sustainability 459 | Debt Indicators 460 | From Distress to Default 463 | A SHORT HISTORY OF SOVEREIGN LENDING DEFAULT 465 | *The 1980s Debt Crisis* 466 | *Causes of the Crisis* 467 | *Impact on the Borrowers* 469 | *Escape from the Crisis, for Some Countries* 470 | The Debt Crisis in Low-Income Countries 473 | *Debt Reduction in Low-Income Countries* 474 | *The Heavily Indebted Poor Country Initiative* 475 | ODIIOUS DEBT 476 | DEBT RELIEF IN UGANDA 479 | Emerging Market Financial Crises 480 | *Domestic Economic Weaknesses* 482 | *Short-Term Capital Flows* 484 | *Creditor Panic* 486 | MODEL OF SELF-FULFILLING CREDITOR PANICS 486 | *Stopping Panics* 489 | *Lessons from the Crises* 494 | Summary 496

14

Foreign Aid

499

Donors and Recipients 501 | *What Is Foreign Aid?* 501 | Who Gives Aid? 503 | THE MARSHALL PLAN 503 | THE COMMITMENT TO DEVELOPMENT INDEX 507 | *Who Receives Foreign Aid?* 512 | *The Motivations for Aid* 514 | CHINA'S FOREIGN AID 515 | Aid, Growth, and Development 518 | *View 1. Although Not Always Successful, on Average, Aid Has a Positive Impact on Economic Growth and Development* 520 | CONTROLLING RIVER BLINDNESS IN SUB-SAHARAN AFRICA 524 | *View 2. Aid Has Little or No Effect on Growth and Actually May Undermine Growth* 526 | FOOD AID AND FOOD PRODUCTION 528 | *View 3. Aid Has a Conditional Relationship with Growth, Stimulating Growth Only Under Certain Circumstances, Such as in Countries with Good Policies or Institutions* 533 | Donor Relationships with Recipient Countries 535 | *The Principal-Agent Problem* 536 | *Conditionality* 537 | *Improving Aid Effectiveness* 540 | Summary 543

15

Managing Short-Run Crises in an Open Economy

545

Equilibrium in a Small, Open Economy 546 | *Internal and External Balance* 547 | REAL VERSUS NOMINAL EXCHANGE RATES 550 | *The Phase Diagram* 553 | *Equilibrium and Disequilibrium* 556 | PIONEERING STABILIZATION: CHILE, 1973–84 559 | *Stabilization Policies* 560 | Applications of the Australian Model 564 | *Dutch Disease* 564 | RECOVERING FROM MISMANAGEMENT: GHANA, 1983–91 566 | *Debt Repayment Crisis* 567 | *Stabilization Package: Inflation and a Deficit* 569 | THE GREEK DEBT CRISIS OF 2010–12 571 | *Drought, Hurricanes, and Earthquakes* 574 | Summary 575 | Appendix to Chapter 15: National Income and the Balance of Payments 576

PART FOUR

Agriculture, Trade, and Sustainability

16

Agriculture and Development

583

Unique Characteristics of the Agricultural Sector 584 | Structural Transformation 587 | Two-Sector Models of Development 590 | *The Labor Surplus Model* 591 | SURPLUS LABOR IN CHINA 598 | *The Neoclassical Two-Sector Model* 599 | DEBATES OVER SURPLUS LABOR 602 | Evolving Perspectives on the Role of Agriculture in Economic Growth and Poverty Alleviation 604 | *Agriculture and Economic Growth* 604 | THE NUTRITION LINKAGE TO ECONOMIC GROWTH 608 | *Agriculture and Poverty Alleviation* 610 | *Agricultural Growth as a Pathway out of Poverty* 613 | Summary 617

17

Agricultural Development: Technology, Policies, and Institutions

619

Characteristics of Traditional Agriculture and Agricultural Systems 620 | *Agricultural Systems* 621 | Diagnosing the Constraints to Agricultural Development 622 | Raising the Technical Ceiling 627 | *The Green Revolution* 628 | *Recent Trends in Agricultural Productivity* 632 | A MODEL OF INDUCED TECHNICAL CHANGE IN AGRICULTURE 635 | Raising the Economic Ceiling 637 | *Food Production Analysis* 638 | *What to Produce? The Product-Product Decision* 638 | *How to Produce It? The Factor-Factor Decision* 641 | *How Much to Produce? The Factor-Product Decision* 643 | FERTILIZER SUBSIDIES IN MALAWI 645 | *Market Access* 651 | CELL PHONES AND AGRICULTURAL DEVELOPMENT 651 | Institutions for Agricultural Development 653 | Land Reform 656 | The World Food Crisis of 2005–08 658 | *Causes of the Crisis* 659 | *Consequences of the Crisis* 661 | Summary 663

18

Trade and Development

665

Trade Trends and Patterns 667 | *Who Trades?* 671 | Comparative Advantage 674 | *The Benefits of Trade* 677 | *Winners and Losers* 681 | Trading Primary Products 683 | EMPIRICAL EVIDENCE ON PRIMARY EXPORT-LED GROWTH 687 | *Export Pessimism* 688 | *Declining Terms of Trade?* 690 | *Dutch Disease* 693 | DUTCH DISEASE: A GEOMETRIC PRESENTATION 697 | NIGERIA: A BAD CASE OF DUTCH DISEASE 700 | INDONESIA: FINDING A CURE 702 | *The Resource Trap* 703 | *Breaking the Resource Curse* 705 | Summary 707

Import Substitution 711 | Protective Tariffs 713 | *Import Quotas* 714 | EFFECTIVE RATES OF PROTECTION 715 | Trade Protection and Politics 718 | THE TWO-COUNTRY MODEL WITH A TARIFF 719 | *Production Subsidies* 720 | *Exchange-Rate Management* 722 | *Outcomes of Import Substitution* 724 | Export Orientation 725 | *Removing the Bias against Exports* 727 | *Favoring Exports* 728 | *Building Export Platforms* 730 | IS CHINA'S EXCHANGE-RATE POLICY UNFAIR? 731 | Trade Strategy and Industrial Policy 734 | Trade, Growth, and Poverty Alleviation 736 | *Trade Reforms and Poverty Alleviation* 739 | Key Issues on the Global Trade Agenda 741 | *Increased Global Competition and the Rise of China (and India)* 741 | *Does Outward Orientation Create Sweatshops?* 743 | LABOR ACTIVISTS AND LABOR OUTCOMES IN INDONESIA 746 | *Expanding Market Access* 747 | *Multilateral Trade Negotiations and the WTO* 750 | *Temporary Migration: Another Dimension of International Trade* 753 | Summary 755

Will Economic Growth Save or Destroy the Environment? 759 | Concept and Measurement of Sustainable Development 761 | *Saving for a Sustainable Future* 765 | THE MALTHUSIAN EFFECT OF POPULATION GROWTH ON ADJUSTED NET SAVINGS IN GHANA 768 | Market Failures 769 | *Externalities and the Commons* 770 | Policy Solutions 773 | *Property Rights* 773 | *Government Regulation* 774 | *Taxes, Subsidies, and Payments for Environmental Services* 776 | TAXING WATER POLLUTION IN COLOMBIA 777 | *Marketable Permits* 779 | *Informal Regulation* 781 | Policy Failures 782 | POLICY FAILURES AND DEFORESTATION IN INDONESIA 783 | *Poverty-Environment Linkages* 785 | *Global Climate Change* 792 | Summary 800