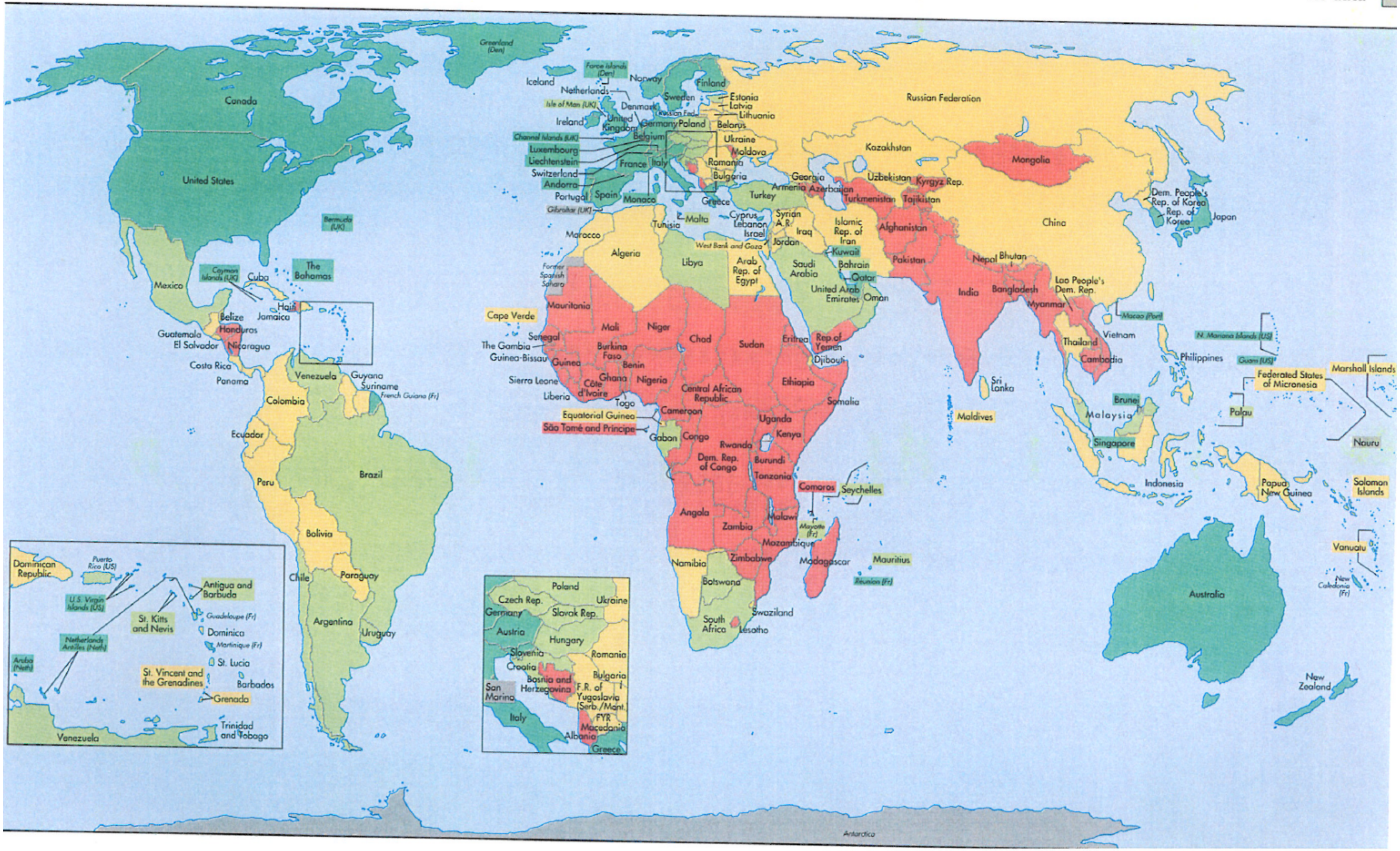
Introduction and Overview

The World by Income

This map presents economies classified according to World Bank estimates of 1997 GNP per capita. Not shown on the map due to space constraints are: American Samoa (upper middle income); Fiji, Kiribati, Samoa, Tonga (lower middle income); French Polynesia (high income); Tuvalu (no data).

Low $785 or less
Lower middle $786 to $3,125
Upper middle $3,126 to $9,655
High $9,656 or more
No data



World Income Distribution

(The figures below refers to year 2015 as in the World Development Report, 2017.)

- **World:** *7.4 billion* people, total income *$76.7 trillion*, average income *$10,440*.
- **Low Income Countries:** World Bank definition: per capita income under $1,025. Many African countries fall under this category, as do countries such as Haiti, Myanmar and Nepal. On the edge: Bangladesh, with $1,190.
  - *638 million* people, total income *$0.4 trillion*, average income *$620*.
- **Low Middle-Income Countries:** Per capita income $1,026–$4,035. Members include India, Nicaragua, Nigeria, and Thailand.
  - *2.9 billion* people, total income *6 trillion*, average income *$2,034*.
- **Upper Middle-Income Countries:** Per capita income $4,036–$12,475. China, richer Latin American economies, such as Argentina and Brazil; countries such as Lebanon, South Africa and Turkey.
  - *2.5 billion* people, total income *$20.7 trillion*, average income *$8,100*.

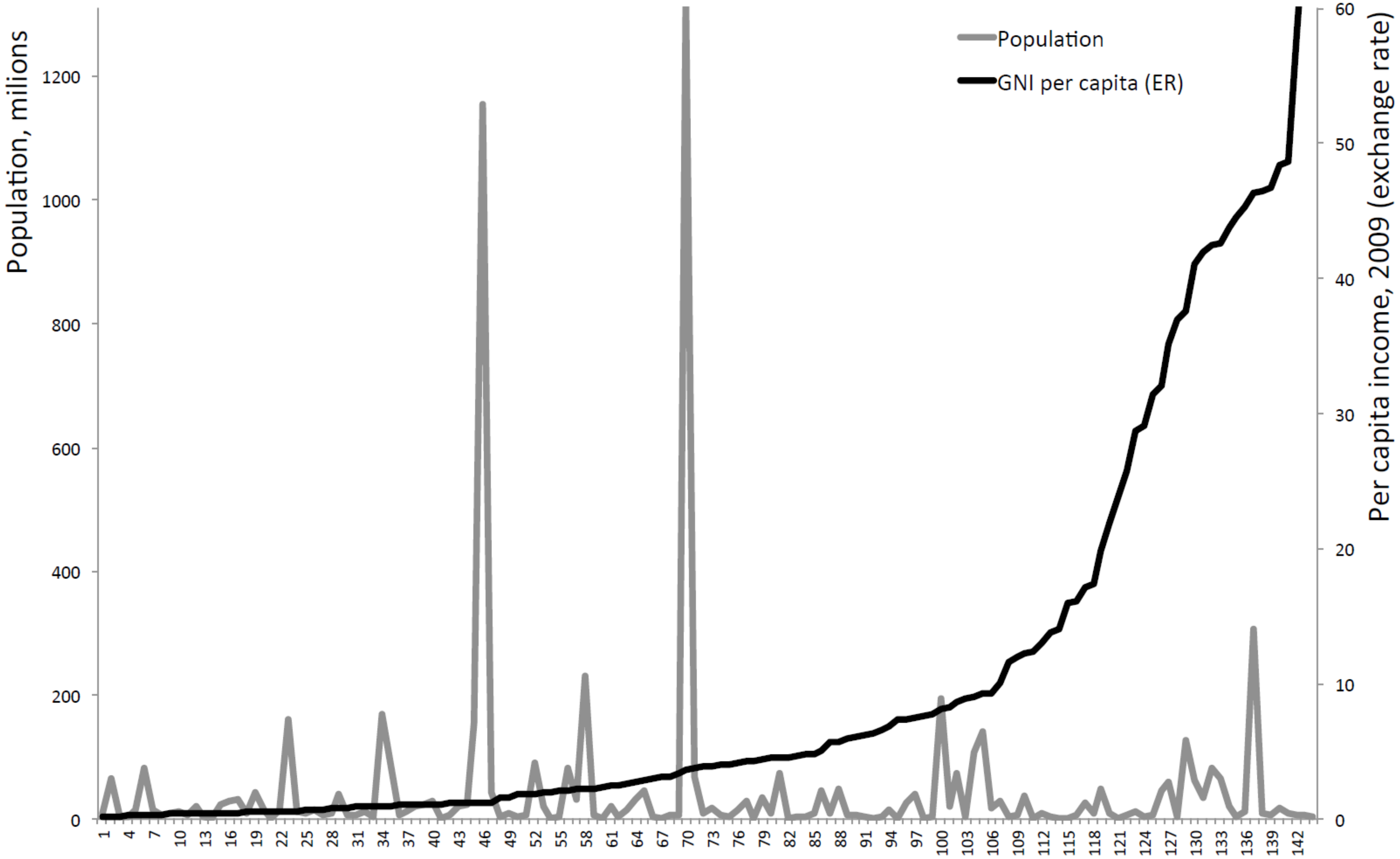
- **High Income Countries:** Per capita income above \$12,475. US, Western and Northern Europe, Japan, Singapore, some Middle East countries.
  - *1.2 billion* people, total income *\$49.4 trillion*, average income *\$41,350*.

- There is little doubt that the distribution of income across the world's nations is extraordinarily skewed.
  - Out of the \$76.7 trillion of world production in 2015, only \$6.4 trillion (8.3%) came from the low and low middle income developing countries;
    - ○ a pittance when we see that these countries house 47.8% of world's population.

  → **48% of the world's population have access to around 8% of world income.**

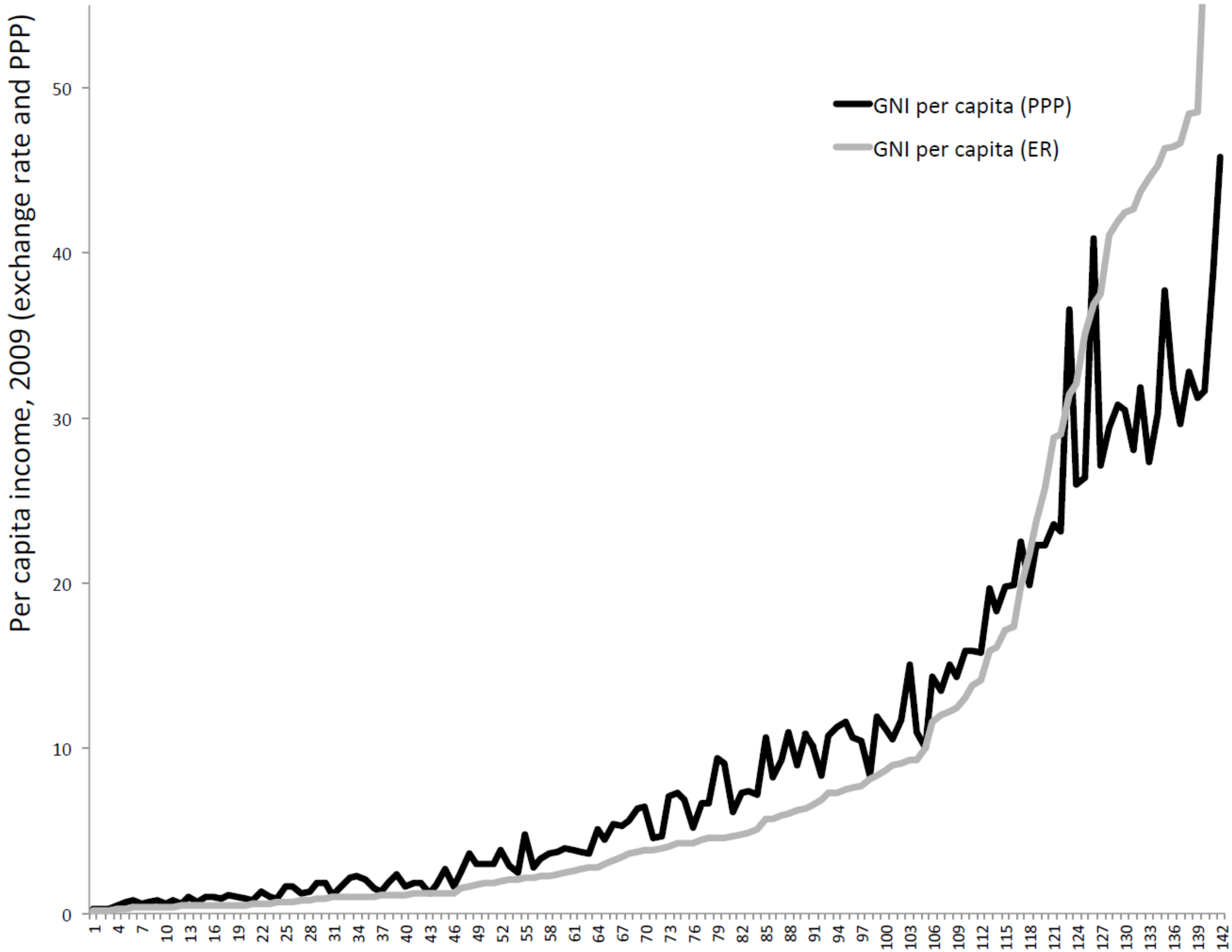
- Norway, the world's richest country, enjoyed a per capita income (\$93,820) that was 225 times the per capita income of the Democratic Republic of Congo, the world's poorest, and close to 80 times the per capita income of Bangladesh.

Population and per capita GDP (exchange rate method), 2009.

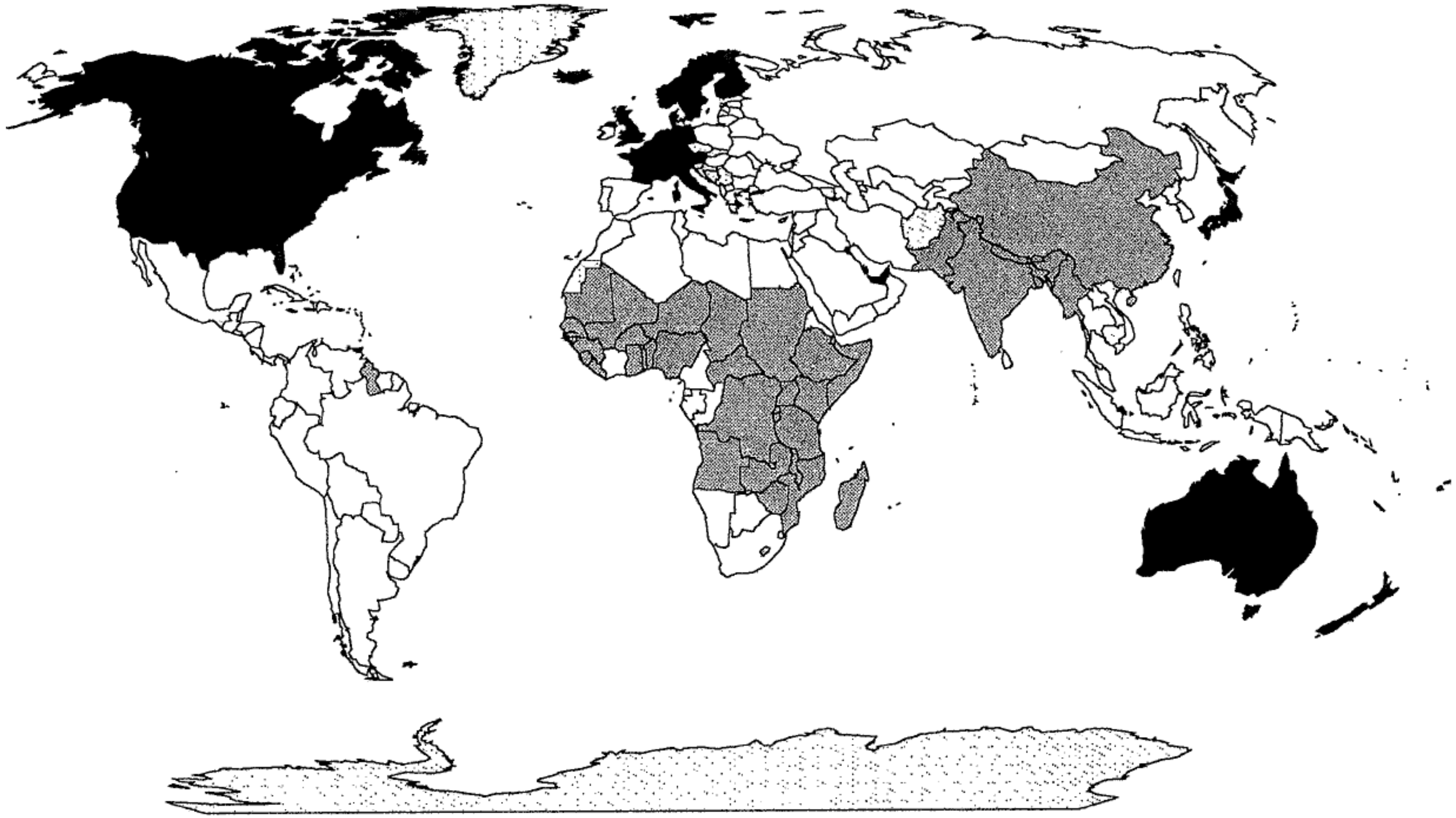


- An index of income that controls for purchasing power (Purchasing Power Parity, PPP) would place these numbers far closer together:
  - World Production (2009): $66.6 trillion
  - High income countries: $35.6 trillion
  - Low and middle income countries: $31 trillion
- The per-capita disparities are enormous, and no amount of fine-tuning in measurement method can get rid of the stark inequalities that we live with.

PPP versus exchange-rate GDP per capita, 2009.

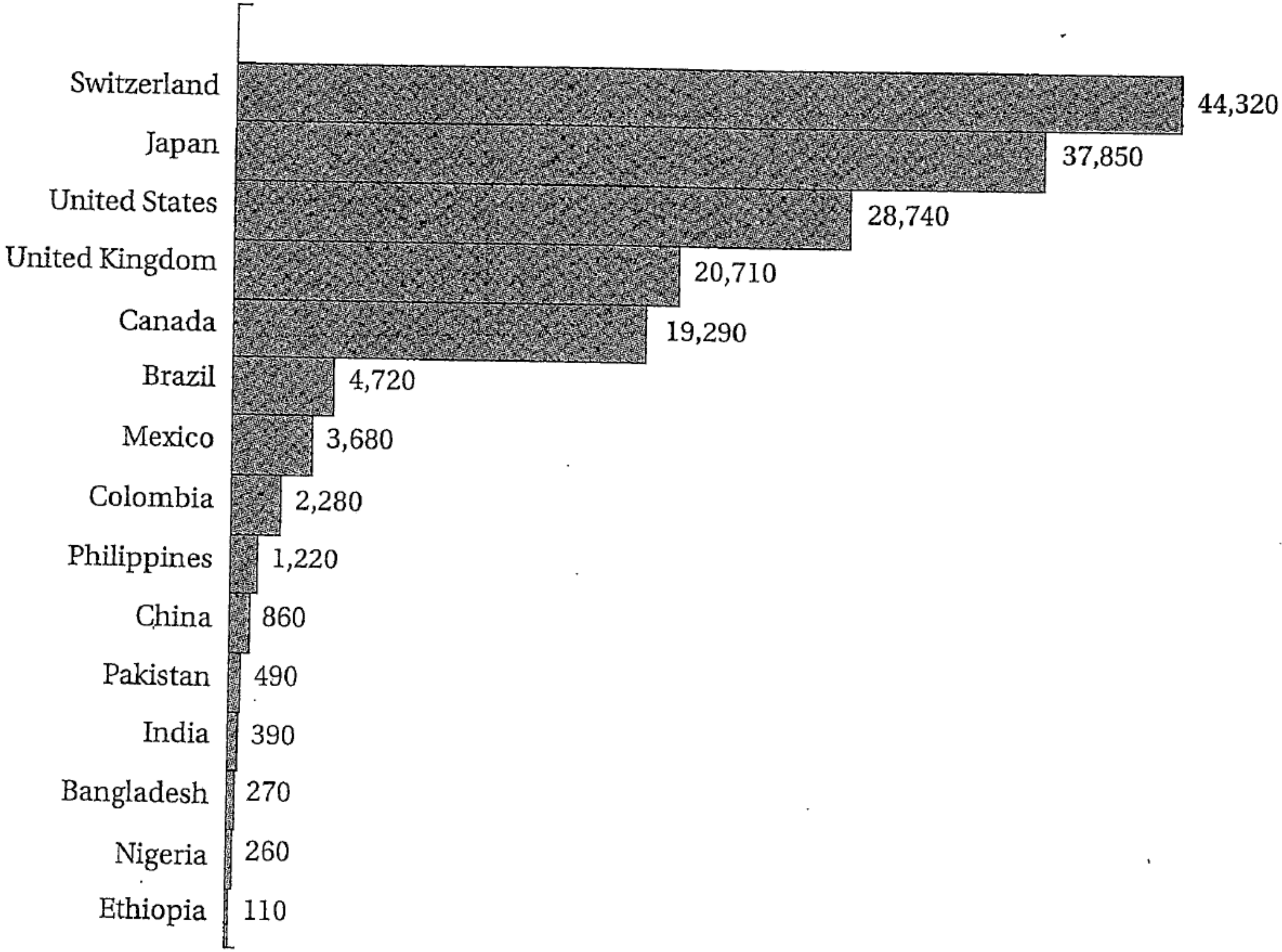


Map 1. The Rich and the Poor



The countries in black contain 15 percent of world population but produce 50 percent of world GDP.
The countries in gray contain 50 percent of world population but produce 14 percent of world GDP.

Figure 2.2 Per Capita Gross National Product in Selected Countries, 1997 (in U.S. dollars at official exchange rates)



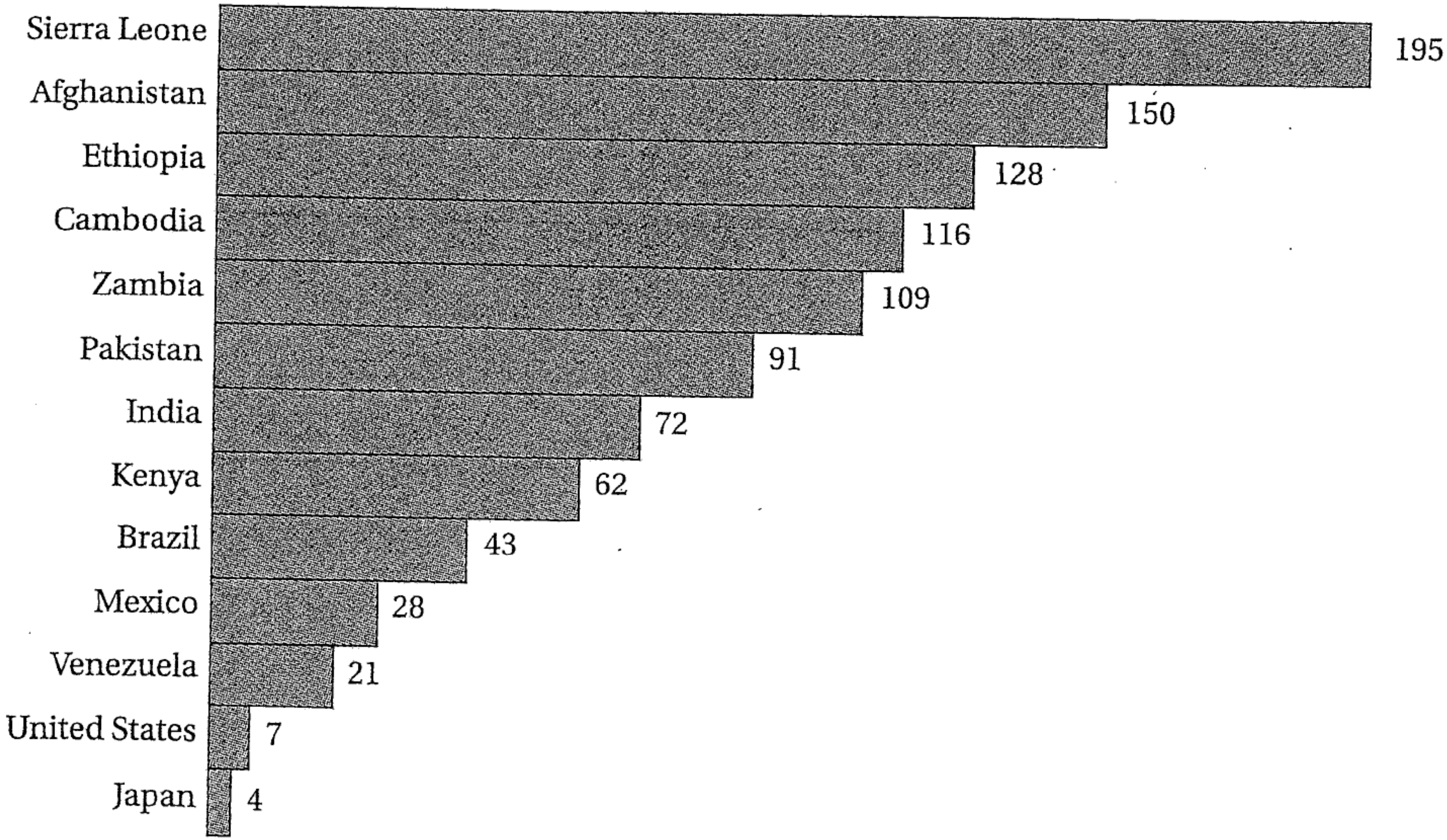
Source: World Bank, *World Development Report, 1998/99: Knowledge for Development* (New York: Oxford University Press, 1998), tab. 1. Reprinted with permission.

Table 2.6 Global Income Disparity between the Richest and Poorest 20 Percent of the World's Population, 1960–2000

	Ratio of Income Shares
Year	Richest to Poorest
1960	30 to 1
1970	32 to 1
1980	45 to 1
1991	61 to 1
2000	70 to 1

Sources: United Nations Development Program, *Human Development Report, 1992* (New York: Oxford University Press, 1992), p. 36; United Nations Development Program, *Human Development Report, 1994 and 2001* (New York: Oxford University Press, 1994 and 2001).

Figure 2.3 Infant Mortality Rates in Selected Countries, 1998 (per 1,000 live births)



Source: Population Reference Bureau, *1998 World Population Data Sheet* (Washington, D.C.: Population Reference Bureau, 1998). Reprinted with permission.

This Course

- Outline and understand the current frontiers of research in *development macroeconomics* that is devoted to broader conceptual themes in development economics, and economy-wide perspectives on the nature of the development "problem".
  - Tries to address the "big questions" of economic development:
    - Why are some countries poor while others are rich?
    - What explains the success stories of economic development, and how can we learn from the failures?
    - How do we make sense of the enormous inequalities that we see both within and across countries?
- Different in approach with *development microeconomics* that digs below and dipper the macro questions.
  - Unearth insights and structures with more confidence than we can hope to have at the world or cross-country level.

Development from the Viewpoint of Convergence

- We begin with the traditional framework of development – defined by conventional growth theory.
- **Convergence:**

  Given certain parameters, say savings or fertility rates, economies inevitably move towards some steady state. If these parameters are the same across economies, then, in the long run, all economies converge to each other.

  - By the law of diminishing returns to capital, poor capital-scarce countries should exhibit higher rates of returns to capital.
    - Consequently, assuming that savings and fertility rates are the same across countries, per capita income in poor countries should grow faster, and eventually living standards in all countries must converge.
  - Reversing the argument, if disparities between rich and poor countries persist over time (see, e.g., Quah (1996) and Pritchett (1997)), it must be because other things, such as savings and population growth rates, are not equal.

- The cause of persistent differences are laid at the door of "fundamental" or "exogenous" variation across countries. These "parameters" range
  - from variables that no one would question are endogenous in some deeper analysis such as fertility and savings rate,
  - through variables that some genuinely believe are exogenous such as corruption, traditions, culture and political climate,
  - to less disputed fundamental variables such as geography or climate.

- Suggests a fundamental belief that the world economy is ultimately a great leveller.
  - If the levelling is not taking place, we must search for that explanation in "parameters" that are somehow structurally rooted in a society.
- Suggests that societies are somehow basically different – with regard to underlying attitudes, preferences or culture, and these account for their differences in economic development.
  - May believe that Confucianism or the Protestant ethic breeds economic success.
  - May be argued that the feudal *zamindari* system in West Bengal was inimical to the development of entrepreneurship.

Development from the Viewpoint of Nonconvergence

- A very different way of asking the “big questions”.
  - Not grounded in any presumption of convergence.
- **Historically conditioned divergence:**

  No fundamental differences across people of different societies. Two societies with the same fundamentals can evolve along very different paths depending on
  - past expectations,
  - aspirations,
  - actual history.
- Some of the best-known economists drawn to this view:
  - Young (1928)
  - Nurkse (1953)
  - Leibenstein (1957)
  - Myrdal (1957)

- Historical legacies need not be limited to a nation's inheritance of capital stock or GDP from its ancestors.
  - Various diverse factors may serve as initial conditions with a long reach:
    - the distribution of economic or political power,
    - legal structure,
    - traditions,
    - group reputations,
    - colonial heritage,
    - specific institutional settings.
  - Factors that have received special attention in the literature include
    - historical inequalities,
    - nature of colonial settlement,
    - character of early industry and agriculture,
    - early political institutions.

Expectations and Development

- Rosenstein-Rodan (1943) and Hirschman (1958) argued that economic development could be thought of as a massive **coordination failure**:

  Several investments do not occur simply because other complementary investments are similarly depressed in the same bootstrapped way.

  – One might conceive of two (or more) equilibria *under the very same fundamental conditions*, “ranked” by different levels of investment.

- Such “ranked equilibria” rely on the presence of **complementarity**:

  A particular form of externality in which taking of an action by an agent increases the marginal benefit to other agents from taking a similar action.

- The **multiple equilibria** are driven by alternative degrees of optimism or pessimism self-justifying these beliefs:

  – Beliefs that a bad outcome will occur do come true, in the sense that such beliefs precipitate the bad outcome.

Aspirations and Development

- The aspirations of a society are conditioned by its circumstances and history, but they also determine its future.

- Aspirations and frustrations are socially generated. It is unclear if this exposure leads to betterment or to despair.

- There is scope
  - for a self-sustaining *failure of aspirations* and economic outcomes,
  - for ever-progressive *growth in aspirations* and economic outcomes.

- The Indian General Elections of 2014:
  - "[The previous term is one] in which growth accelerated, Indians started saving and investing more, foreign investment came rushing in, [and] poverty declined sharply . . . [But] growth can also unleash powerful aspirations as well as frustrations, and political parties who can tap into these emotions reap the benefits." Ghatak-Ghosh-Kotwal, *Economic and Political Weekly*, April 19, 2014
  - "[P]eople with dramatically raised but mostly unfulfillable aspirations have become vulnerable to demagogues promising national regeneration. It is this tiger of unfocused fury . . . that Modi has sought to ride from Gujarat to New Delhi." Mishra, *The Guardian*, May 16, 2014
- "The French found their position all the more intolerable as it became better." de Tocqueville, 1856

History: Inequality and Markets

- History-Dependence:

  Historically given initial conditions can persistently influence current outcomes, thereby reinforcing historical legacies.

- Historical inequalities persist (or widen) because each individual entity – dynasty, region, country – is swept along in a self-perpetuating path of occupational choice, income, consumption, and accumulation.

- The relatively poor may be limited in their ability to invest productively both in themselves and in their children.
  - Such investments might include both
    - physical projects such as starting a business, or
    - "human projects" such as nutrition, health and education.
  - The poor may have ideas that they cannot profitably implement as it requires startup funds that they do not have.

- Faced with a different level of initial inequality, the very same economy may perform very differently.
  - Investment opportunities are available widely through the population,
  - A new outcome emerges with not just lower inequality, but higher aggregate income.
- These are different steady states, and they could well be driven by distant histories.

History: Political and Legal Institutions

- In many developing countries, the early institutions of colonial rule were directly set up for the purposes of surplus extraction.
  - Variation depending on
    - whether the areas were sparsely or densely populated to begin with, or
    - whether there was large-scale availability of mineral deposits.
  - Resource deposits favoured large-scale extractive industry.
    - Example: Many parts of South America.
  - Soil and weather conditions might encourage plantation agriculture, often with the use of slave labor.
    - Example: The Caribbeans.
  - High preexisting population density would favour extraction of a different kind: the setting-up of institutional systems to acquire rents.
    - Example: The British colonial approach in large parts of India.

- In contrast, where initial settlements did not go hand in hand with systems of tribute, land grants, or large-scale extractive industries, one might expect comparative equality and a subsequent path of development that is more broad-based.
  - Example: North America, Australia, New Zealand.
- Sokoloff and Engerman (2000):

  "... initial conditions had lingering effects ... because government policies and other institutions tended to reproduce them. Specifically, in those societies that began with extreme inequality, elites were better able to establish a legal framework that insured them disproportionate shares of political power, and to use that greater influence to establish rules, laws, and other government policies that advantaged members of the elite relative to nonmembers contributing to persistence over time of the high degree of inequality. ... In societies that began with greater equality or homogeneity among the population, however, efforts by elites to institutionalize an unequal distribution of political power were relatively unsuccessful ..."

References

- This note is based on

1. Ray, Debraj (2008), “Development Economics”, in *The New Palgrave Dictionary of Economics*, edited by L. Blume and S. Durlauf,

   and

2. Mookherjee, Dilip and Debraj Ray (2000), Introduction to *Readings in the Theory of Economic Development*, London: Blackwell.

  – The references mentioned in this note can be traced in these two articles.