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# Introduction and Overview

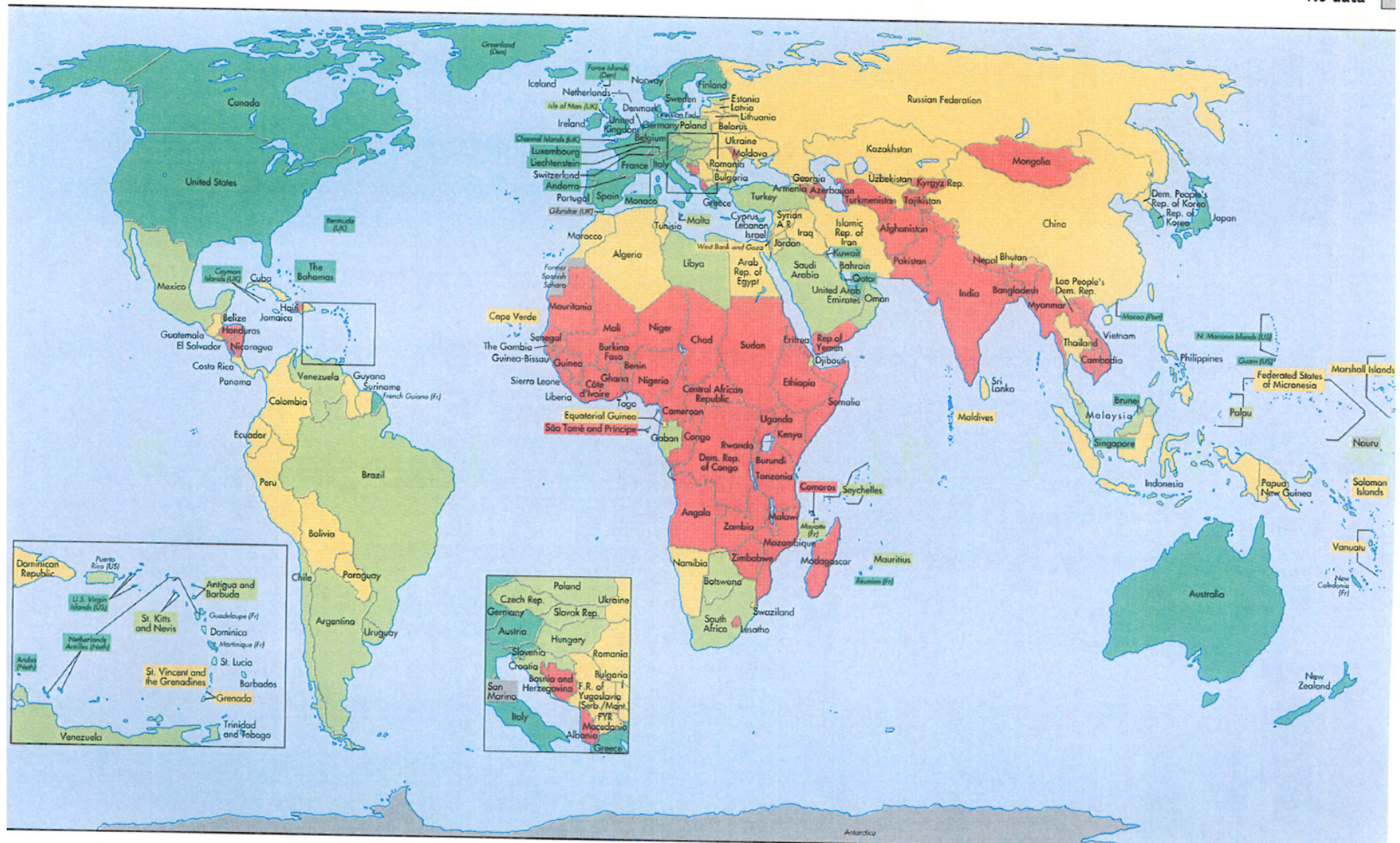
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## The World by Income

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

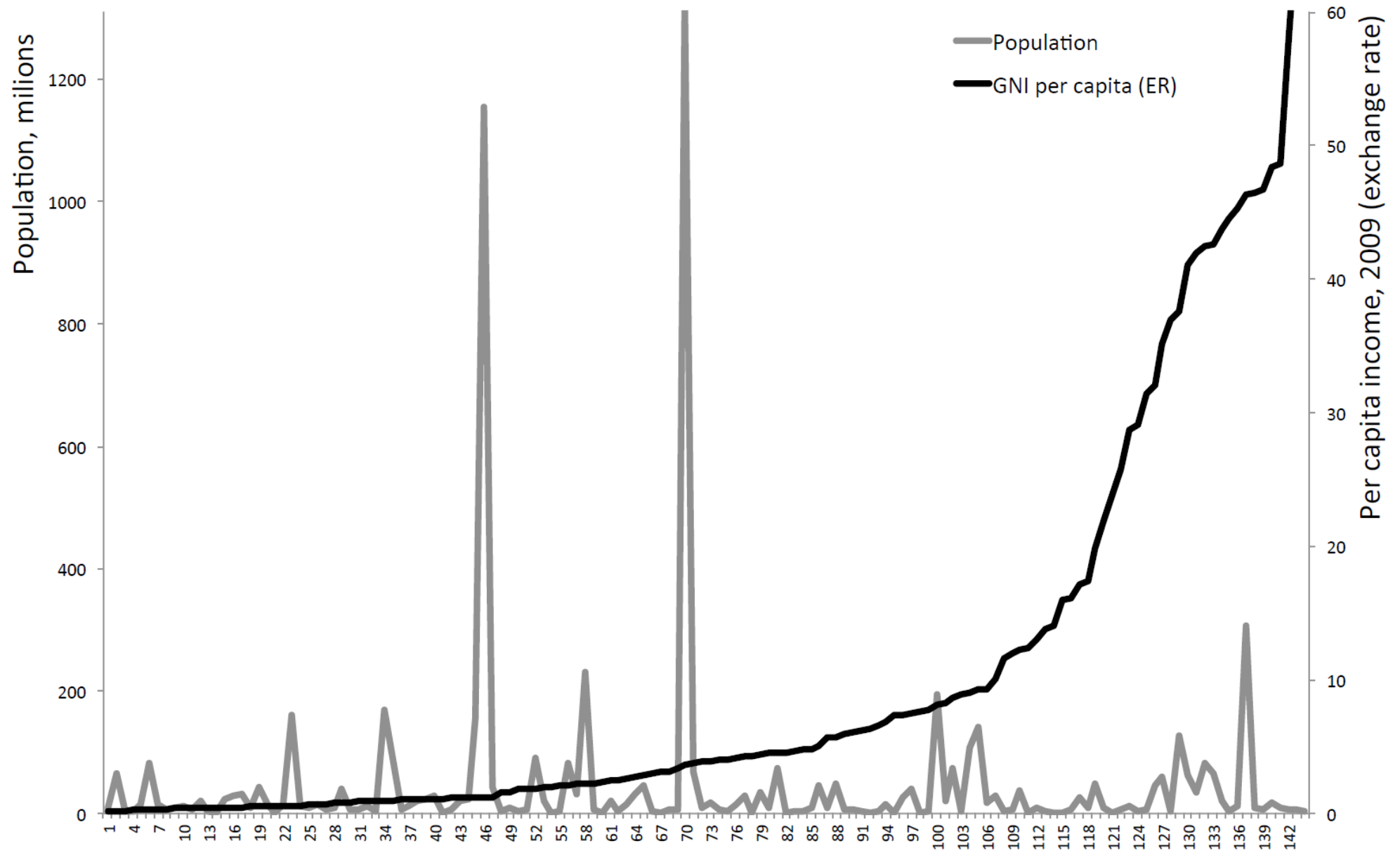
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(The figures below refers to year 2020 as in the World Development Report, 2022.)

- **World:** *7.75 billion* people, total income *\$84.4 trillion*, average income *\$10,900*.
- **Low Income Countries:** World Bank definition: per capita income under \$1,035. Many African countries fall under this category, as do countries such as Afghanistan, Myanmar and Nepal. Around upper edge: Tajikistan, Tanzania.
  - *665 million* people, total income *\$0.55 trillion*, average income *\$827*.
- **Low Middle-Income Countries:** Per capita income \$1,036–\$4,045. Include India, Nicaragua, Nigeria, and Thailand. Around upper edge: Indonesia, the Philippines.
  - *3.33 billion* people, total income *7.33 trillion*, average income *\$2,200*.
- **Upper Middle-Income Countries:** Per capita income \$4,046–\$12,535. China, richer Latin American economies (Argentina and Brazil), Lebanon, South Africa, Turkey. Around upper edge: Costa Rica, Mauritius.
  - *2.51 billion* people, total income *\$23.1 trillion*, average income *\$9,200*.

- **High Income Countries:** Per capita income above \$12,535. US, Western and Northern Europe, Japan, Singapore, some Middle East countries.
  - *1.21 billion* people, total income *\$53.26 trillion*, average income *\$44,020*.
- There is little doubt that the distribution of income across the world's nations is extraordinarily skewed.
  - Out of the \$84.4 trillion of world production in 2020, only \$7.88 trillion (9.3%) came from the low and low middle income developing countries;
    - a pittance when we see that these countries house 51.5% of world's population.
  - **51% of the world's population have access to around 9% of world income.**
- Switzerland, the world's richest country, enjoyed a per capita income (\$86,601) that was 150 times the per capita income of the Democratic Republic of Congo (\$557), the world's poorest, and 44 times the per capita income of Bangladesh (\$1,968).

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

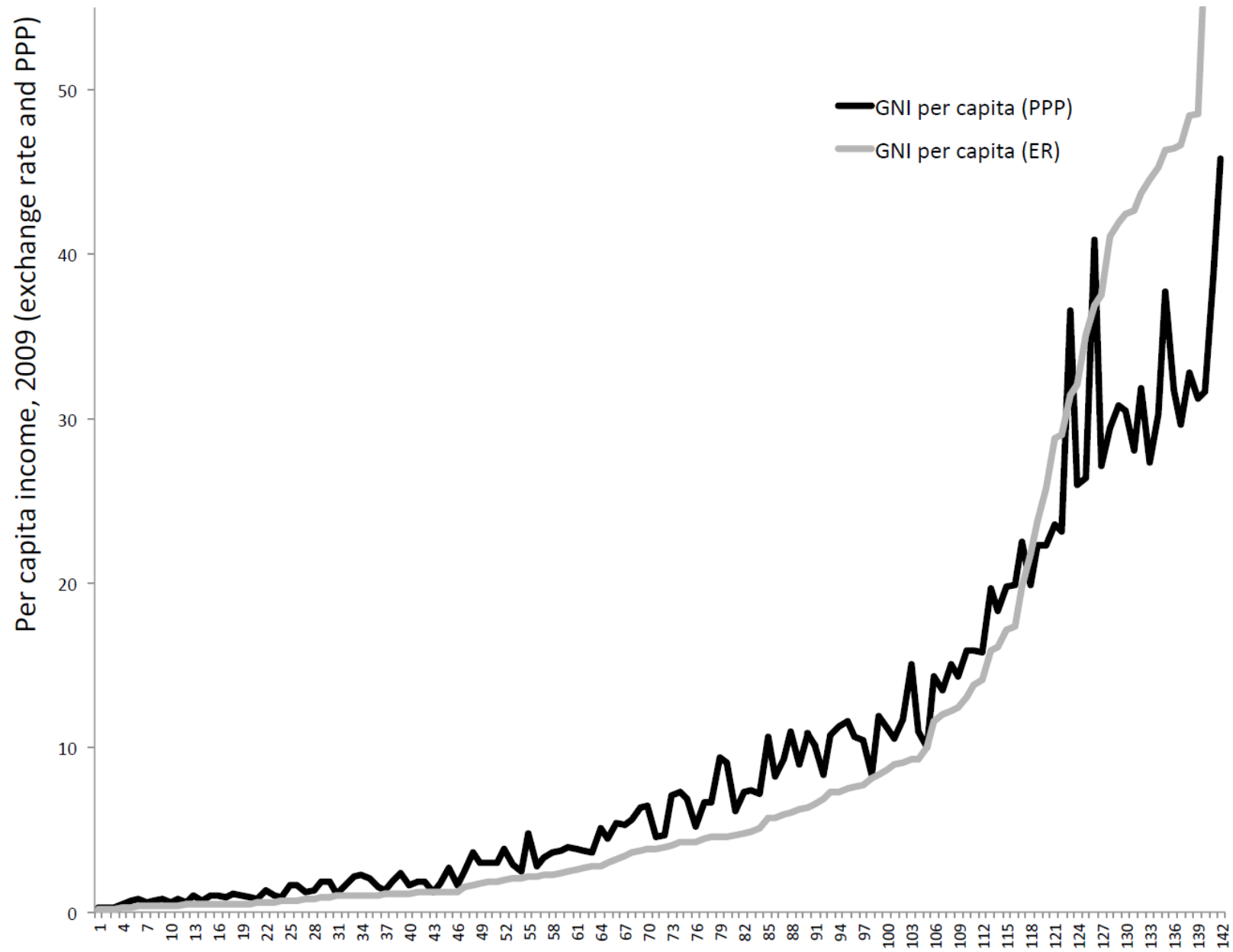




- **Corrections:**

- *Underreporting* of income (tax evasion, subsistence production);
  - *Distorted pricing* (monopolies or oligopolies, public sector enterprises);
  - *Externalities*: pollution, environmental damage, resource depletion.
- 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.



## **The Magnitude of the Problem:**

- Poor countries are very poor indeed.
  - 61.2% of the population in Mali in the 2001 lived on less than \$1.25 a day at 2005 PPP prices and 86.4% in Nigeria lived under \$2 a day in 1996-1997.
- This translates into
  - 30% of the children under 5 in Mali in 2000-2007 had measurable signs of malnutrition (44% in India, 0 in Sweden);
  - Under 5 mortality rate in Mali was 217/1000 in 2006 (270 in Sierra Leone, 4 in Norway);
  - Life expectancy at birth for males was 52 years in Mali (41 years in Sierra Leone, 79 in Sweden);
  - 76% of adults were illiterate in Mali in 2005 (61% in Niger, 0 in Sweden).



- The *Poverty Line* in India is 16 rupees per person and per day (2005).
  - This is also the average poverty line for the 50 countries where most of the poor live.
- 16 rupees is 36 cents (US). . . . But life is cheap in India, so if we correct for world prices, it corresponds to 99 cents (this is what we mean when we talk about “life under a dollar a day”):
  - The poverty line in the US is 14 dollars per day.
  - Average GDP per capita in the US is \$47,400, implying \$130 per person per day!
- **865 million people in the world live with less than 99 cents per day in 2005.**

- Poverty is not only lack of income, but also
  - Poor health:
    - 9 million children every year die under the age of 5, mainly of diseases that could have been prevented;
      - 6.5 million children die every year before their first birthday;
    - 27 million children every year do not get the essential vaccinations.
  - Poor education: 50% of children enrolled in schools in India cannot read a simple paragraph.
  - Poor quality of life: hours collecting water instead of playing, working, learning.
  - Difficulty to realize your ambition: Get a loan for a business; be insured for the risk of your farm.
- **Amartya Sen: Development as Freedom.**

## The Story of Abu

- From *A Quiet Violence*, by Betsy Hartmann and James Boyce, 1983.
  - A quasi-journalistic account by two economists of life in rural Bangladesh, in 1975.
    - These were the worst years in the history of Bangladesh. Things have gone much better since.
  - This is the story of one peasant family.
- The First Visit:
  - Abu is sick. He has not been able to work for the last three weeks.
  - His children are hungry.
  - His oldest daughter, who is still a child, is the only earner in the family. She gets 1/4 kilo of rice for husking rice all day.
  - Abu cannot afford the Rs. 100 that he needs to pay a doctor.

- The Past:

- Abu used to have enough land to live on, but he needed money to take care of his mother who was sick, and sold some of the land.
  - She died any way.
- They had a number of children and the land they had was no longer enough to feed everyone.
- When there was no food, they borrowed from the money lender at very high rates, which ate into their future income.
- Abu started working for a landlord who gives one meal and 1.25 kilos of rice a day.
- He could sharecrop and get to keep half of what he grows but he gets it after the harvest and in the meanwhile they starve.
  - Also renting a plough-team costs 2 days labor/day.
  - He had to mortgage more land to his landlord.

- The Future:
  - At the first visit they are still optimistic.
    - Abu had planted a jackfruit tree four years ago.
    - In a couple of years it will yield fruits that can be sold and bring in good money.
- The Second Visit:
  - Abu has sold land to pay the doctor.
  - His wife has no work.
  - In the lean season he cannot find work either, so they are starving.
  - Abu cuts down a jackfruit tree and sells the wood for 25 takas.
    - It never got a chance to bear fruit.

## **Is the vicious circle completely closed?**

- Should you take away from the story of Abu that there is no need to take this course: as long as people are poor they will be sick and as long as they are sick they will be poor?
  - In fact, there are many examples where the vicious circle can be broken: many interventions could durably help Abu and others.
  - Development economics is largely about this question: how do vicious circles emerge and what can we do about them?

# Topics to be Covered in this Course

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- **Introduction:**

- We look at some stylized facts based on micro-level studies as to how the poor live.
  - Special focus on their consumption, income generation, as well as their access to markets and public services.
- This motivates our theoretical discussion of the microeconomic studies of various markets and institutions that affect development.



- **Agricultural Organization and Productivity in Developing Countries:**

- Agriculture occupies a central place in less developed economies. We study
  - features of agricultural organization in these economies, such as *sharecropping*, *tenancy* and *interlinked contracts*, as optimal second-best responses to missing markets and transactions costs,
  - strategies for successful agrarian reform,
  - empirical determinants of organizational and contractual form,
    - and the effect of these on agricultural productivity.

- **Credit Markets in Developing Countries: Theory and Evidence:**

- Credit markets play a crucial role in economic development by allowing those who have talents and skills but not money, to undertake investments by using the surplus savings of others.
- If this market is subject to frictions, then worthwhile projects may not be undertaken for lack of money, thereby depressing national income below its potential.
- We study theoretical models of frictions in financial markets, empirical evidence on their importance, and innovative policy interventions in response to financial market imperfections, with special emphasis on micro-finance.

- **Micro Finance:**

- Microfinance is one of the key elements of development policy.
  - We look at theoretical models of how microfinance works as a mechanism, and also empirical studies of its impact.

- **Property Rights:**

- Property rights are at the heart of a market economy and some trace the problem of underdevelopment as a problem of imperfect property rights.
- We examine various mechanisms through which property rights affect economic efficiency and also look at empirical studies that study the impact of them in the context of some reform.

- **Social Networks and Informal Institutions:**

- Even though formal institutions of enforcing property rights and contracts are weak or non-existent in developing countries, informal institutions based on repeated interactions have emerged in response.
- We draw on theoretical work on the benefits and costs of informal institutions and complement it with empirical work drawing on economic history, as well as contemporary developing countries.

- **Education: Private and Public Education Choice:**

- Effective provision of public goods is a key determinant of quality of life.
  - Access to safe drinking water, sanitation, transport, medical care, and schools is essential both as a direct component of well-being and as an input into productive capability.
- The rich have the option to seek private alternatives, lobby for better services, or, if need be, move to a different area. The poor frequently do not.
- Mechanisms for effective delivery of public goods and services, particularly to the poor, are therefore central to any development strategy.

- **Discrimination and Affirmative Action:**

- When choosing which students to admit, employees to hire, candidates to slate, or firms to patronize,
  - the social identity of those selected – that is, an agent's race, sex, age, nationality, religion, ethnicity, or caste – can be a matter of great importance.
- As a consequence, regulations intended to achieve more diversity in the ranks of the chosen – “affirmative action” – have been promulgated in many societies throughout the world.
- We will examine the welfare economics of such diversity-promoting public regulations.

## ● The Political Economy of Development:

- The textbook paradigm of economywide development rests on the premise of “balanced growth”.
- In many developing countries, economic growth has been fundamentally **uneven**. First one sector, then another, then a third have grown rapidly *but not all together*.
- The question really is not whether growth is balanced – it isn’t – but whether the abstraction is a useful one.
- For many important development questions, we believe the answer is no.
- This is why we would like to take the reality of “uneven growth” seriously and use it as an organizing device for a research program.

# The Game Plan

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- This semester is about building blocks.
  - Household behavior (nutrition, health, education);
  - Markets (land; credit; savings; insurance);
  - Institutions (formal and informal).
- In the Development Macroeconomics course next semester we will incorporate these building blocks in good models to answer the “big questions”.