Development Economics
Theory and practice

Alain de Janvry and Elisabeth Sadoulet
# Contents

List of figures  xi  
List of tables  xix  
Preface  xxiii  
Acknowledgments  xxv  

## INTRODUCTION

### 1 WHAT IS DEVELOPMENT? INDICATORS AND ISSUES

- Seven Dimensions of Development  30  
- Income and Income Growth  31  
- Poverty and Hunger  37  
- Inequality and Inequity  44  
- Vulnerability to Shocks  49  
- Basic Needs: Human Development  52  
- Sustainability in the Use of Natural Resources  59  
- Quality of Life  67  
- Development Goes Beyond Income, But Can Income Growth Deliver Development?  69  
- Conclusion: Development Is Multidimensional, So Can We Agree on What  70  

### 2 THE STATE OF DEVELOPMENT

- Income Growth and the Convergence Club  79  
- Poverty and Hunger  80  
- Inequality  88  
- Basic Human Needs  94  
- Sustainability in Resource Use  99  
- Quality of Life  102  
- Conclusion  105  

### 3 HISTORY OF THOUGHT IN DEVELOPMENT ECONOMICS

- Introduction: Why History Matters  113  
- Basic Principles in Analysing the History of Thought in Development Economics  114  
- Selected Schools of Thought in Development  116  
- The Digital Revolution and the Future of Convergence  120  
- Conclusion  140  

CONTENTS

6 INEQUALITY AND INEQUITY 248
DESCRIPTING AND MEASURING INEQUALITY 249
DECOMPOSING INEQUALITY 253
RELATIONSHIP BETWEEN LEVEL OF INCOME (GDP\textsubscript{pc}) AND INEQUALITY: EMPIRICAL EVIDENCE ON THE KUZNETS INVERTED U-CURVE 255
THE ALVAREDO-ATKINSON-PIKETTY-SAEZ CRITIQUE 257
IMPACT OF GDP\textsubscript{pc} GROWTH ON POVERTY AND INEQUALITY 258
IMPACT OF INEQUALITY ON GROWTH: NINE CAUSAL CHANNELS 263
CAN GREATER INEQUALITY BE A SOURCE OF EFFICIENCY GAINS? 270
WHAT ROLES FOR ETHNIC FRACTIONALIZATION AND GENETIC DIVERSITY? 272
WHAT ROLE FOR EQUITY IN DEVELOPMENT? 274
INCLUSIVE GROWTH 275
CONCLUSION: THE GROWTH-INEQUALITY-POVERTY DEVELOPMENT TRIANGLE 276

7 INTERNATIONAL TRADE AND INDUSTRIALIZATION STRATEGIES 284
TRADE OPENNESS 285
GAINS FROM TRADE: WHY COUNTRIES TRADE, BUT NOT EVERYONE GAINS 288
ABSOLUTE, COMPARATIVE, AND COMPETITIVE ADVANTAGE 293
TRADE POLICY AND INDICATORS OF PROTECTION 296
USING TRADE POLICY FOR DEVELOPMENT: TARIFFS AND SUBSIDIES 300
DYNAMIC GAINS FROM TRADE: IMPORT-SUBSTITUTION INDUSTRIALIZATION AS A POLICY GAMBLE 303
TRADE AND INDUSTRIALIZATION STRATEGIES: HOW TO CHOOSE? 306
IS TRADE GOOD FOR GROWTH? 310
IS TRADE GOOD FOR POVERTY REDUCTION? 313
TRADE AND THE ENVIRONMENT 315
TRADE AND FOOD SECURITY 319
DECLINE OF THE WTO AND THREATS TO MULTILATERALISM 321

8 EXPLAINING ECONOMIC GROWTH: THE MACRO LEVEL 326
THE GROWTH PUZZLE 327
GENERIC MODELING OF INCOME GROWTH 327
CAPITAL ACCUMULATION FOR GROWTH: THE HARROD-DOMAR MODEL 330
PRODUCTIVITY GROWTH AND FACTOR DEEPENING: GROWTH ACCOUNTING IN THE SOLOW MODEL 334
THE ROLE OF AGRICULTURE IN GROWTH: STRUCTURAL TRANSFORMATION 341
THE ROLE OF AGRICULTURE IN GROWTH: DUAL-ECONOMY MODELS 343
THE ROLE OF AGRICULTURE IN GROWTH: OTHER MODELS 348
APPENDIX 8.1: SOLUTION TO THE SOLOW GROWTH MODEL 355

9 ENDOGENOUS ECONOMIC GROWTH 359
EXPLAINING GROWTH 359
THE COORDINATION PROBLEM IN GROWTH 362
<table>
<thead>
<tr>
<th>CONTENTS</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>STRUCTURAL DETERMINANTS OF GROWTH</td>
<td>366</td>
</tr>
<tr>
<td>BEHAVIORAL DETERMINANTS OF GROWTH</td>
<td>372</td>
</tr>
<tr>
<td>CONCLUSION</td>
<td>375</td>
</tr>
<tr>
<td><strong>10 INTERNATIONAL FINANCE AND DEVELOPMENT</strong></td>
<td>379</td>
</tr>
<tr>
<td>EXCHANGE RATES AND DEVELOPMENT</td>
<td>379</td>
</tr>
<tr>
<td>COUNTRY CURRENCIES</td>
<td>380</td>
</tr>
<tr>
<td>DEFINITIONS: NOMINAL, REAL, AND REAL EFFECTIVE EXCHANGE RATES</td>
<td>381</td>
</tr>
<tr>
<td>EXCHANGE-RATE REGIMES</td>
<td>385</td>
</tr>
<tr>
<td>IMPACT OF A CHANGE IN THE RER ON REAL BALANCES</td>
<td>390</td>
</tr>
<tr>
<td>THREE EXAMPLES OF EXCHANGE-RATE SHOCKS</td>
<td>393</td>
</tr>
<tr>
<td><strong>11 POPULATION AND DEVELOPMENT</strong></td>
<td>403</td>
</tr>
<tr>
<td>DEFINITIONS: DEMOGRAPHIC CONCEPTS</td>
<td>404</td>
</tr>
<tr>
<td>SOME DATA FOR WORLD POPULATION</td>
<td>410</td>
</tr>
<tr>
<td>HISTORY OF WORLD POPULATION AND DEMOGRAPHIC TRANSITION</td>
<td>412</td>
</tr>
<tr>
<td>CAUSES OF POPULATION GROWTH</td>
<td>413</td>
</tr>
<tr>
<td>POPULATION POLICY</td>
<td>422</td>
</tr>
<tr>
<td>OTHER ISSUES IN POPULATION AND DEVELOPMENT</td>
<td>427</td>
</tr>
<tr>
<td><strong>12 LABOR AND MIGRATION</strong></td>
<td>432</td>
</tr>
<tr>
<td>LABOR AND EMPLOYMENT</td>
<td>433</td>
</tr>
<tr>
<td>RURAL-URBAN MIGRATION</td>
<td>436</td>
</tr>
<tr>
<td>IMPACTS OF MIGRATION</td>
<td>451</td>
</tr>
<tr>
<td>CONCLUSION</td>
<td>459</td>
</tr>
<tr>
<td><strong>13 FINANCIAL SERVICES FOR THE POOR</strong></td>
<td>463</td>
</tr>
<tr>
<td>THE MICROFINANCE REVOLUTION</td>
<td>464</td>
</tr>
<tr>
<td>THE GENERIC-LENDER PROBLEM</td>
<td>465</td>
</tr>
<tr>
<td>COMMERCIAL BANKS</td>
<td>467</td>
</tr>
<tr>
<td>LOCAL MONEYLenders, OR &quot;USURERS&quot;</td>
<td>469</td>
</tr>
<tr>
<td>INFORMAL MICROFINANCE INSTITUTIONS: ROSCAS</td>
<td>470</td>
</tr>
<tr>
<td>MICROFINANCE WITH GROUP LENDING</td>
<td>472</td>
</tr>
<tr>
<td>VILLAGE BANKS AND SELF-HELP GROUPS</td>
<td>475</td>
</tr>
<tr>
<td>MFIs WITH INDIVIDUAL LOANS: PROXIMITY LENDING</td>
<td>477</td>
</tr>
<tr>
<td>LOCAL SOURCES OF CREDIT BASED ON INTERLINKAGES IN VALUE CHAINS</td>
<td>477</td>
</tr>
<tr>
<td>OTHER ISSUES IN MICROFINANCE LENDING</td>
<td>478</td>
</tr>
<tr>
<td>CAN THE POOR BE INSURED? THE PROMISE OF INDEX-BASED WEATHER INSURANCE</td>
<td>483</td>
</tr>
<tr>
<td>CAN THE POOR SAVE? OFFERING SAVINGS OPPORTUNITIES AND INCENTIVES</td>
<td>490</td>
</tr>
<tr>
<td>FACILITATING MONEY TRANSFERS</td>
<td>494</td>
</tr>
<tr>
<td>CONCLUSIONS ON MFIs: HOW USEFUL ARE THEY FOR POVERTY REDUCTION?</td>
<td>494</td>
</tr>
<tr>
<td><strong>14 SOCIAL-ASSISTANCE PROGRAMS AND TARGETING</strong></td>
<td>501</td>
</tr>
<tr>
<td>SOCIAL ASSISTANCE IN POVERTY-REDUCTION STRATEGIES</td>
<td>502</td>
</tr>
<tr>
<td>A TYPOLOGY OF SOCIAL-ASSISTANCE PROGRAMS</td>
<td>504</td>
</tr>
</tbody>
</table>
THE TARGETING OF SOCIAL PROGRAMS: BENEFITS AND COSTS 509
ERRORS IN TARGETING: EXCLUSION (TYPE I) AND
INCLUSION (TYPE II) ERRORS 510
TARGETING METHODS 512
QUALITY OF TARGETING 522
TRADE-OFFS IN TARGETING 523
USING SOCIAL-SAFETY-NET (SSN) PROGRAMS FOR EFFICIENCY
GAINS AND GROWTH 528
IMPACT EVALUATION OF SOCIAL PROGRAMS: SOME EXAMPLES 530

15 SUSTAINABLE DEVELOPMENT AND THE ENVIRONMENT 538
LINKS BETWEEN DEVELOPMENT, RESOURCE CONSERVATION,
AND ENVIRONMENTAL SUSTAINABILITY 539
NEGATIVE EXTERNALITIES 542
INCOMPLETE PROPERTY RIGHTS 550
PUBLIC GOODS 552
DISCOUNTING: PRIVATE VS. SOCIAL, AND EXPONENTIAL VS.
HYPERBOLIC 553
THE SUSTAINABILITY OBJECTIVE 556
DILEMMAS IN THE ENVIRONMENT-DEVELOPMENT RELATION 557
INTRODUCING NEW MARKETS: PAYMENTS
FOR ENVIRONMENTAL SERVICES 560

16 COMMON PROPERTY RESOURCES AND DETERMINANTS
OF COOPERATION 566
WHY ARE THERE COMMON PROPERTY RESOURCES? 567
ECONOMICS OF CPR USE 569
GROUNDS FOR PESSIMISM ABOUT COOPERATIVE BEHAVIOR 570
COORDINATE OUTCOMES IN NON-COOPERATIVE GAMES 572
DETERMINANTS OF COOPERATION AND COLLECTIVE ACTION 577
WHY SECURE PROPERTY RIGHTS OVER LAND MATTER FOR
ECONOMIC DEVELOPMENT 583
BEHAVIORAL GAMES IN DEVELOPMENT ECONOMICS 584

17 HUMAN CAPITAL: EDUCATION AND HEALTH 593
WHY ARE EDUCATION AND HEALTH IMPORTANT FOR DEVELOPMENT? 594
INDICATORS AND STATUS OF EDUCATION 595
WHAT DETERMINES THE LEVELS OF SCHOOLING? 599
RETURN TO EDUCATION 607
CCT PROGRAMS: OPORTUNIDADES AS A CASE STUDY 609
INDICATORS AND STATUS OF HEALTH 612
WHAT DETERMINES HEALTH ACHIEVEMENTS? 616
IMPACT OF HEALTH ON DEVELOPMENT OUTCOMES 621
HEALTH POLICIES 624

18 AGRICULTURE FOR DEVELOPMENT 634
AGRICULTURE FOR DEVELOPMENT 635
THE STATE OF WORLD AGRICULTURE 642
DETERMINANTS OF AGRICULTURAL GROWTH 650
FOOD SECURITY IN DEVELOPING COUNTRIES 665
THE POLITICAL ECONOMY OF AGRICULTURE FOR DEVELOPMENT 669
## CONTENTS

### 19 DEVELOPMENT AID AND ITS EFFECTIVENESS 675

**Overview** 676
Aid in a Historical Perspective 677
The Evolution of Foreign Aid 681
Fungibility of Foreign Aid 683
Aid Effectiveness from a Macro Perspective 685
Evaluating the Impact of Foreign Aid from a Micro Perspective 689
The Practice of Foreign Aid 690
Aid Strategies for Greater Effectiveness: What Can Be Done? 696
The Debate on Foreign Aid 699
Conclusion: Toward a New Aid Architecture 702

### 20 INSTITUTIONAL INNOVATIONS AND DEVELOPMENT 710

Institutions and Development 710
Assumptions Underlying the New Institutional Economics 712
Market Failures Induced by Transaction Costs 713
Institutional Responses to Market Failures 716
Mechanisms of Institutional Change 716
An Example of Institutional Choice: Sharecropping Contracts 720
Other Examples of Institutional Innovations that Help Reduce Transaction Costs and/or Compensate for Market Failures 730

### 21 POLITICAL ECONOMY AND THE ROLE OF THE STATE 737

Introduction 737
The Functionalist State 740
The Pluralist State: Public Choice 745
Economics of Public Authority: Rent-Seeking, Political Influence, and Corruption 758
Seven Strategies to Limit Rent-Seeking 763
Public Expenditures and Development: The Role of Infrastructure 768

### 22 THE ECONOMICS OF FARM HOUSEHOLDS 776

Importance of Farm Households 777
Definitions of Farm Households 780
Farm-Household-Behavior Models 785
Responses to Market Signals: Separability 788
Net Buyers, Net Sellers, and Food Security 790
Access to Land: The Role of Land Reform 792
Can the Family Be Competitive and Survive 795
Risk and Self-insurance in Household Behavior 802
Intra-Household Allocation of Resources and Gender Roles 805

Index 813