

# Economic Development, Growth and Welfare

**ECONOMICS TODAY**  
Edited by Andrew Leake

The *Economics Today* series surveys contemporary headline topics in applied economics. Each book in the series is written by an expert in the field in a style that is fluently readable. It serves the student of introductory economic principles while also making the subject accessible to a more general reader. The series embraces the problem-solving skills of the new generation of students and stresses the importance of real-world issues and the significance of economic ideas.

*Published*

Andrew Leake: **The Economic Question**  
Jean-Louis Barsoux and Peter Lawrence: **The Challenge of British Management**  
Andy Beharrell: **Unemployment and Job Creation**  
Frank Burchill: **Labour Relations**  
Kenneth Durham: **The New City**  
S.F. Goodman: **The European Community (2nd edn)**  
Charles Smith: **Economic Development, Growth and Welfare**  
Jenny Wales: **Investigating Social Issues**  
John Wigley and Carol Lipman: **The Enterprise Economy**  
Margaret Wilkinson: **Taxation**

*Forthcoming*

Nigel Healey and Mark Cook: **Growth and Structural Change**  
Ian Hodge and Diane Dawson: **Choices for the Environment**  
Kent Matthews: **Macroeconomics and the Market**  
John Wigley: **The Rebirth of Russia**

**Series Standing Order**

If you would like to receive future titles in this series as they are published, you can make use of our standing order facility. To place a standing order please contact your bookseller or, in case of difficulty, write to us at the address below with your name and address and the name of the series. Please state with which title you wish to begin your standing order. (If you live outside the UK we may not have the rights for your area, in which case we will forward your order to the publisher concerned.)

Standing Order Service, Macmillan Distribution Ltd,  
Houndmills, Basingstoke, Hampshire, RG21 2XS, England.

**ECONOMIC  
DEVELOPMENT,  
GROWTH AND  
WELFARE**

**Charles Smith**

**M**  
MACMILLAN

© Charles Smith 1994

All rights reserved. No reproduction, copy or transmission of this publication may be made without written permission.

No paragraph of this publication may be reproduced, copied or transmitted save with written permission or in accordance with the provisions of the Copyright, Designs and Patents Act 1988, or under the terms of any licence permitting limited copying issued by the Copyright Licensing Agency, 90 Tottenham Court Road, London W1P 9HE.

Any person who does any unauthorised act in relation to this publication may be liable to criminal prosecution and civil claims for damages.

First published 1994 by  
THE MACMILLAN PRESS LTD  
Houndmills, Basingstoke, Hampshire RG21 2XS  
and London  
Companies and representatives  
throughout the world

ISBN 978-0-333-59268-7      ISBN 978-1-349-23385-4 (eBook)  
DOI 10.1007/978-1-349-23385-4

A catalogue record for this book is available  
from the British Library.

Typeset by Cambrian Typesetters, Frimley

Dedicated to: Francis Archie Smith, Mary Louise Quibell,  
José Brocca Ramón, and Rosa García López; my  
grandparents, *mis abuelos*

Make John Lennon's dream come true . . .  
It's the least we can do.

Song by Gerry Murray (Brandon Publishers), performed by Christie Moore  
(WEA Records).

# Contents

<b>List of Tables, Figures and Boxes</b>	<b>x</b>
<b>Acknowledgements</b>	<b>xiii</b>
<b>Preface</b>	<b>xiv</b>
<b>List of Abbreviations</b>	<b>xvii</b>
<b>1 The World and its Welfare</b>	<b>1</b>
Income, Growth and Welfare	2
<b>2 Development: Economic and Human</b>	<b>14</b>
Economic Development	15
Human Development?	16
How and Why does Development Take Place?	22
Development Policy	28
<b>3 Population Growth: Threat or Opportunity?</b>	<b>29</b>
Supply and Demand	29
Population Pressures	30
The Prophet of Doom	32
The Case for Population Growth	34
The Case Against	35
The Dependency Ratio	36
Social Attitudes	37

Population Control	37
Children in the Population	38
The Development Trap	40
The Malthusian Trap	41
<b>4 Can we Cure Poverty?</b>	<b>43</b>
Who are the Poor?	43
Too Poor to Live?	45
How to Cure Poverty?	45
Aid and Absolute Poverty	46
Poverty and the Environment	46
Relative Poverty	47
Income and Wealth	48
How Can We Measure Income Inequality?	50
Why do Poorer Countries Seem Prone to Disaster?	53
Disease and Famine	55
The Rural Poor and Empowerment	58
Poverty and the Role of Women	59
<b>5 Feeding the World</b>	<b>63</b>
Nutrition and Cash	63
Terms of Trade	64
The Banks	65
The Advisors	65
Local Effects	66
Land-ownership	67
The Green Revolution	68
Land Degradation	70
Cash Crops and the MDCs	70
Alternatives to Cash Crops	73
What Can the MDCs Do?	75
What Can the LDCs Do?	76
Food and Water	76
<b>6 Industrialisation – The Key to Development?</b>	<b>78</b>
The Stages of Growth	78
Structural Change	80



	<b>The Dual-Sector Development Model</b>	<b>82</b>
	<b>Criticism of the Lewis Model</b>	<b>87</b>
	<b>The Myrdal Theory</b>	<b>88</b>
	<b>The Todaro Model</b>	<b>88</b>
	<b>The Role of Government</b>	<b>89</b>
	<b>Rural versus Urban: A False Dichotomy?</b>	<b>90</b>
	<b>Appropriate Technology</b>	<b>90</b>
	<b>Multinational Enterprises</b>	<b>94</b>
	<b>MNEs and LDCs</b>	<b>95</b>
<b>7</b>	<b>Life in a Trading World</b>	<b>98</b>
	<b>Industry and Trade</b>	<b>98</b>
	<b>Export-Orientation (Outward Strategy)</b>	<b>99</b>
	<b>Import-Substitution (Inward Strategy)</b>	<b>100</b>
	<b>Trade and Welfare</b>	<b>101</b>
	<b>Why does Trade Take Place?</b>	<b>108</b>
	<b>Free Trade versus Protectionism</b>	<b>111</b>
	<b>Trade and the LDCs</b>	<b>113</b>
<b>8</b>	<b>The Debt Crisis</b>	<b>124</b>
	<b>Currency and Exchange Rates</b>	<b>124</b>
	<b>International Saving, Investing and Borrowing</b>	<b>128</b>
	<b>Aid</b>	<b>141</b>
<b>9</b>	<b>Government, Externalities and the Environment</b>	<b>147</b>
	<b>Macroeconomic Policy</b>	<b>147</b>
	<b>Microeconomic Policy</b>	<b>149</b>
	<b>Types of Planning</b>	<b>149</b>
	<b>Externalities</b>	<b>151</b>
	<b>Natural Monopolies, Public Goods and Merit Goods</b>	<b>152</b>
	<b>Centralisation and Decentralisation</b>	<b>153</b>
	<b>Areas of Special Government Concern</b>	<b>154</b>
	<b>Some Conclusions</b>	<b>156</b>
	<b>Index</b>	<b>159</b>

# List of Tables, Figures and Boxes

## Tables

- 2.1 The Human Development Index and Other Indicators for Selected Countries, 1992 18
- 2.2 Main HDI Rankings, 1993 20
- 2.3 Education as Investment: Economic Rates of Return on Education 25
- 3.1 The World's Largest Cities, 1985 and 2000 31
- 4.1 Poverty in LDCs 44
- 8.1 Aid Receipts 145
- 9.1 The Effects of Externalities 152

## Figures

- 1.1 A Production Possibility Curve 6
- 2.1 Spending on Education 24
- 3.1 World Population Projections 30
- 3.2 Infant Mortality Rate (children under 5) 40
- 3.3 Main Causes of Death of Children under 5, in Developing Countries, 1990 41
- 4.1 World Income Distribution: A World Lorenz Curve, 1990 50
- 4.2 World Income Distribution: Income Disparities over Time 52

4.3	Projected New HIV Infections each year	56
4.4	Daily Calorie Supply per Head as a Percentage of Requirements	57
5.1	Supply and Demand for Sugar	67
5.2	Price Stabilisation through Buffer Stocks	73
5.3	Tobacco Sales in MDCs and LDCs	74
6.1	Percentage Shares of Output in MDCs	81
6.2	The Lewis Model	86
7.1	International Trade and Economic Welfare: A Closed Economy	102
7.2	International Trade and Economic Welfare: An Open Economy	103
7.3	The Welfare Effects of a Tariff	105
7.4	The Welfare Effects of an Import Quota	107
7.5	The Welfare Effects of a Government Intervention Purchasing Scheme	108
7.6	The Welfare Effects of a 'Setaside' or Production Quota Scheme	110
7.7	Supply and Demand – Commodities and Manufactures	114
7.8	Regional Blocs and World Trade	116
7.9	Sri Lanka Tea Exports	122
8.1	Net FDI Flows to Developing Countries	129
8.2	Net FDI Flows from OECD Investors, 1980–89	130
8.3	Three Major Sources of FDI Flows to Development Countries	132
8.4	FDI Flows to Developing Countries: Regional Trends, 1980–89	133
8.5	East Asia and the Pacific: The Principal Sources of Direct Investment Flows, 1980–89	134
8.6	East Asia and the Pacific: The Principal Destinations of FDI Flows	135
8.7	Latin America and the Caribbean: The Principal Sources of Direct Investment Flows, 1980–89	136
8.8	Latin America and the Caribbean: The Principal Destinations of Direct Investment Flows	137
8.9	World Bank Lending (as at 30 June 1991)	138
8.10	Money Flows between the IMF, World Bank and LDCs	144

**xii** *List of Tables, Figures and Boxes*

**Boxes**

6.1 Case Study: Finance in Mauritius	83
6.2 Case Study: The Durable Car Company	93
7.1 Case Study: The Tin Collapse	118
8.1 An Example of an IMF Programme	131
8.2 Examples of World Bank Loans	138
8.3 The Debt Boomerangs	142

# Acknowledgements

I wish to thank Stephen Rutt and the publishing team for supporting this project, and Andrew Leake for his encouragement and advice. All errors and omissions are my own responsibility.

I particularly wish to record my thanks to Julia, Sally and Matthew Smith for their patience and understanding; and my apologies to Charles and Olga Smith, Glyn and Peg Kingdom, and anyone else I might have neglected during my hours at the word processor.

The author and publishers wish to thank the following copyright-holders and sources of statistical information for permission to reproduce copyright material: Bank of England, Organisation for Economic Co-operation and Development, Oxfam, United Nations Development Programme, United Nations Children's Fund, World Bank, World Health Organisation, *Finance and Development*, *New Internationalist*. Every effort has been made to contact copyright-holders for permission to reproduce material in this book, but if any have been inadvertently overlooked, the publishers would be pleased to make the necessary arrangement at the earliest opportunity.

# Preface

Development economics has a reputation for being a particularly difficult branch of an already difficult subject. This is partly due to the fact that textbooks on development tend to be either encyclopaedic works for degree students, or in-depth studies of narrow topics aimed at the high-level specialist. In contrast, this book is meant to be an 'entry-level' text, suitable for economics candidates at A-level (where development is likely to increase in importance as syllabuses adopt an 'issues based' approach); and also suitable for equivalent examinations such as the International Baccalaureate (where development is already an important part of the curriculum). Additionally, it should be useful to students of related subjects, such as geography; to undergraduates embarking on a study of development; and to the general reader.

It is therefore hoped that this little book will have something of value for young economists who wish to be shown ways in which their chosen subject is of vital importance in the real world; for teachers who wish to give higher priority to development topics; and for readers of all ages who wish to take an informed interest in these important issues.

In a book of this size it is not possible to address all development issues in detail, and so some selection has taken place. An attempt has been made to address those aspects of development which relate to the themes of 'growth' and 'welfare'; and to discuss issues which give the student of introductory economics a chance to see

some applications of basic economic theory, and to use the language of economics in a development context.

Readers wishing to continue their interest in development with further reading can safely afford to avoid most of the British tabloid press, where reporting of foreign news tends to range in standard from non-existent to appallingly xenophobic. It is no wonder that so many readers of most examples of this genre appear to have difficulty in regarding themselves as Europeans, let alone as world citizens. Of the broadsheet papers, *The Financial Times* can be singled out for its regular in-depth surveys of particular countries, and *The Independent*, *The Observer* and *The European* often focus on particular development issues. The 'EG' supplement of the education section of *The Guardian* very often contains a great deal of useful information, of interest to both teachers and students. Probably the most efficient way of keeping in touch with development issues is to follow the themes presented in the weekly newspaper, *The Economist* and the monthly *New Internationalist*, and I think that it is fair to say that these journals view matters from rather different political stances.

Somewhat in advance of anticipated changes in the A-level economics syllabuses, the editors of *The Economic Review* and *Economics and Business Education* (formerly *Economics*) show commendable willingness to carry articles covering development topics. It is to be hoped that this healthy trend will continue, and that students will be encouraged to follow the new opportunities to study development economics which should become available in the near future.

Among official publications I would strongly recommend the World Bank's *World Development Report* and the United Nations Development Programme's *Human Development Report*, whose findings feature strongly in parts of this book. These are annual publications, and something which makes them particularly interesting is the way in which they usually deal with a particular theme each year.

On BBC Radio 4, programmes such as *Analysis* and *From Our Own Correspondent* sometimes touch on development issues. While there are occasional emotional appeals at the time of some obvious disaster, mainstream television largely ignores the less developed countries (LDCs). The so-called 'minority' channels are honourable exceptions. It is particularly worth seeking out

relevant Open University programmes on BBC2, and any repeats of the excellent *One World* series screened on Channel 4 during the 1992 Rio Summit Conference on the Environment.

A book of limited size and scope has to be selective in its approach. During the important gestation period, I found the aforementioned sources of great value in helping me to select some themes and issues as being particularly worth highlighting in this book.

I hope that students using this book will find themselves just a little better-equipped to follow development issues, wherever they are discussed, with a critical awareness.

*Bridgend, Wales*

CHARLES SMITH



# List of Abbreviations

bn	billion
m	million
CAFOD	Catholic Fund for Overseas Development
CAP	Common Agricultural Policy (EC)
EBRD	European Bank for Reconstruction and Development
EC	European Community (European Union)
EFTA	European Free Trade Association
ERM	Exchange Rate Mechanism
FAO	Food and Agricultural Organisation
FTA	Free Trade Areas
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
GNP	gross national product
HDI	Human Development Index
HDR	Human Development Report
HYV	high-yielding varieties (of cereal)
IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
IFC	International Finance Corporation
IFAD	International Fund for Agricultural Development
IMF	International Monetary Fund
IPPF	International Planned Parenthood Federation

**xviii** *List of Abbreviations*

ITC	International Tin Council
LDCs	less developed countries
MDCs	more developed countries
MEW	measure of economic welfare
MFA	Multi-Fibre Agreement
MFN	most favoured nation
MIGA	Multilateral Investment Guarantee Agency
MNE	multinational enterprise
NAFTA	North Atlantic Free Trade Area
NIC	newly industrialised countries
NSP	net social product
OECD	Organisation for Economic Cooperation and Development
OPEC	Organisation of Petroleum Exporting Countries
OXFAM	Oxford Committee for Famine Relief
PPC	production possibility curve
PPP	purchasing parity
SDR	Special Drawing Rights
TVs	traditional varieties (of crops)
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
UNICEF	United Nations Children's Fund
US	United States (adjective)
USA	United States of America (noun)
VER	voluntary export restraint
WDR	World Development Report
WHO	World Health Organisation