

ECON 611
Spring 2006
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ECONOMIC DEVELOPMENT POLICY

Course Description

Economic Development Policy concerns the nature and consequences of policies designed to promote welfare-augmenting growth and structural change. This requires a micro-analytic perspective that accommodates induced institutional change and a welfare economics suitable for analyzing the static and dynamic consequences of policy reform. Topics include: Specialization and Market Evolution, Economic Justice, Land, Labor, and Credit Policies, the New Institutional Economics, Developing Agriculture and Industry, The Political Economy of Corruption, Sustainable Development, the Asian Miracle and Crisis, the Washington Consensus (before and after Stiglitz) and the Hawaii Synthesis. A central theme will involve contrasting the new Development Microeconomics with the more fundamental New Institutional Economics and New Classical Microeconomics approaches.

Required texts

Mookerjee and Ray, *Readings in the Theory of Economic Development*,

Recommended texts

Bardhan and Udry, *Readings in Development Economics, v. I and v. II.* (2000)

Yang, *Development Economics: Inframarginal vs Marginal Analysis*, Blackwell, 2003

References

Bardhan, Pradhan and Christopher Udry, *Development Microeconomics*, Oxford, 1999

Ray, *Development Economics, Princeton*, 1998

World Bank, *World Development Report, 2006: Equity and Development*, Oxford, 2005.

Chenery & Srinivasan, *Handbook of Development Economics, Vol. 3*, Elsevier

Meier and Rauch, *Leading Issues in Economic Development, 8th ed.*, Oxford, 2005

Stiglitz, *Whither Socialism* (1993) and *Globalization and Discontents* (2002)

Dixit, *The Making of Economic Policy* (1996)

Laffont, *The Theory of Incentives* (2002)

Sen, *Development as Freedom*

Lucas, *Lectures in the Theory of Economic Growth*, 2002.

Grading

Midterm	24%
Paper ¹	24%
Final ²	36%
Homework+citizenship	16%

Office hrs.

¹ Two-page (max) typed proposal due Feb 2. Paper due April 27.

² See *UHM Schedule of Classes*.

Wed, 1:30-3 and by appt.

Tentative Reading List and Topics

I. Welfare-theoretic Foundations of Development Policy

- A. "Welfare Economics and the Minimal Role of Government: An Axiomatic Approach," (handout)
- B. Appendices
 - 1. Arrow, K. (1969), "The Organization of Economic Activity: Issues Pertinent to the Choice of Market versus Non-market Allocation," in the *Analysis and Evaluation of Public Finance: the PPB System*.
 - 2. Cornwall, R. (1984), *The Use of General Equilibrium Analysis*, Amsterdam, North-Holland. pp. 377-388, 461-471, 484-487, 535-536, 556-560*
 - 3. Roumasset, J. (1979), "Sharecropping, Production Externalities, and the Theory of Contracts," *American Journal of Agricultural Economics*, Vol 61, No. 4: 640-647
 - 4. Roumasset, J. (1990), "Debreu-Scarff Version of the Coase Theorem," (An Appendix to Exposure Trading, an East-West Center Working Paper)*
 - 5. Samuelson, P. (1969), "Pure Theory of Public Finance and Taxation"*
 - 6. Proof of 5a <http://ideas.repec.org/a/cje/issued/v31y1998i4p952-974.html> *
- C. Stiglitz, "Some Lessons from the East Asian Miracle," *World Bank Research Observer*, Aug., 1996, esp. pp.160-161; Review of Globalization and its Discontents, <http://www.nybooks.com/articles/15630> ; chs 1-3* and ch 4 (esp sections before discussion of non-convexities) from Stiglitz, *Whither Socialism*.
- D. R'set, "Development is Letting Go of Fear" UH Program on Conflict Resolution, WP 1993-3.
- E. Krugman, "The Fall and Rise of Development Economics"
<http://www.pkarchive.org/theory/dishpan1.html>
- F. Intro and ch 1 of B&U.*
- G. Murphy et. al, "Industrialization and the Big Push," ch 1 in Mookherjee and Ray.
- H. Power, "Role of Protection...", *EAER*, 6/72, esp. history of thought in econ dev.
- I. Chenery (1961), "Comparative advantage and development policy. *American Economic Review*, 51;* Scitovsky, "Two concepts of external economies," *JPE* 62(2), 1954, pp. 143-151*
- J. Ray, Ch. 5*
- K. Lucas, lecture 3; also ch 9 in Bardhan and Udry I and as Lucas, Robert E. (1993): "[Making a miracle](#)." *Econometrica*, 61(2):251-272.³

³ Background reading for Lucas: Arrow, Kenneth J. (1962): "[The economic implications of learning by doing](#)." *Review of Economic Studies*, 29:155-73; Parente, Stephen (1994): "Technology adoption, learning by doing, and economic growth." *Journal of Economic Theory*, 63:346-369; Stokey, Nancy L. (1988): "[Learning by doing and the introduction of new goods](#)." *Journal of Political Economy*, 96:701-717; Young, Alwyn (1991): "[Learning by doing and the dynamic effects of international trade](#)." *Quarterly Journal of Economics*, 106:369-405; Young, Alwyn (1993): "[Invention and bounded learning by doing](#)." *Journal of Political Economy*, 101:443-472; Krugman, Paul M. (1987): "The narrow moving band, the dutch disease and the economic consequences of Mrs. Thatcher. Notes on trade in the presence of dynamic scale economies." *Journal of Development Economics*, 27:41-55.

II. Development Microeconomics I: Behavior

- A. Household decision-making w/transaction costs
- B. Decision-making among low-income farmers
- C. Readings
 1. Ray, ch. 9*
 2. Roumasset, J. (1995), *Behavior and Organization in Developing Agriculture, Part I*, Chs. 2, 3; 4*, 5.
 3. Hutaserani and Roumasset (1991), "Institutional Change and Demographic Transition in Rural Thailand", *EDCC*
 4. de Janvry, Fafchamps, and Sadoulet (1991), "Peasant Household Behavior with missing markets: some paradoxes explained," *Economic Journal* 101: 1400-17 (**Jstor**); or Sadoulet and de Janvry, *Quantitative Development Policy Analysis*, 1995 (Johns Hopkins), ch. 7*; or Key, Sadoulet, and de Janvry, "Transaction Costs and Agricultural Household Supply Response," *AJAE*, 5/00, 246-59
- D. Research topic: Prove conjecture in R'set, ch. 2 and reassess Fafchamps, Key et. al.

III. Development Microeconomics II: Organization

- A. Choice of contracts in space and time
- B. Government intervention in land, labor and credit markets (e.g., land reform, usury laws and insurance)
- C. Induced institutional change
- D. Research topics: Crop insurance revisited; Collateral confusion & the case against land titles
- E. Readings
 1. Ray, Ch. 11-15*
 2. Bardhan and Udry, chs. 4* and 6-9.*
 3. B&U I, chs 2, 6, 7*, and 12.
 3. Hoff, K. et. al. (1993) (eds) *The Economics of Rural Organization: Theory, Practice and Policy*, chs. 4-6, Oxford University Press*
 4. Evenson and Roumasset (1986), "Markets, Institutions and Family Size in Rural Philippine Households," in *Journal of Philippine Development*, Vol 13, No. 23; or Evenson in Quibria*
 5. Handbook, v. 3 (chapters by Binswanger and on Rural Credit)*
 6. Roumasset, J., *Behavior and Organization in Developing Agriculture, Part II*, chs. 4-12 (version of 7 also available as "Explaining Diversity in Agricultural Organization: An Agency Perspective," U. Minnesota Econ Dev Bulletin, 94-3
(http://agecon.lib.umn.edu/cgibin/pdf_view.pl?paperid=1760)
Also "Agricultural Development Thinking: Fads, Fancies, Fallacies, and Frontiers," www.economics.hawaii.edu/research/seminars/05-06/12_02_05.pdf
 7. Roumasset, J. (1995), "The Nature of the Agricultural Firm," JEBO "Agency Costs and the Ag Firm," (w/M. Uy), *Land Econ*, 7/87 (in ch. 7)
 8. Lipton, "Ag. Risk, Rural Credit, and the Inefficiency of Inequality," in R'set et. al., *Risk, Uncertainty, and Ag. Development* (1979)*
 9. James and Roumasset, "Migration and the Evolution of Tenure Contracts

- in Newly-Settled Regions,” *J.Dev.Econ*, 14 (1984), 147-162.
10. Stiglitz, “Economic Organization,” Handbook, vol. I, 115-124 (section on sharecropping)*
 11. R’set, “The Welfare Economics of Rural Credit Markets and the Benefits of land Titles,” report to the World Bank, 1986 and Review of Floro and Yotopoulos, *Informal credit markets and the new institutional economics: the case of Philippine Agriculture* in JEL, 12/92.
 12. Deweaver and R’set, Beyond Stiglitz, A Dynamic Theory of Share Tenancy (see econ department seminar archives and <http://www.economicsbulletin.com/2002/volume15/EB-01O10001A.pdf>).
 13. Singh, “Theories of Sharecropping,” Ch 2 in B&U I*; Conning and Robinson(2005), “Property and the Political Organization of Agriculture” (note stylized facts) <http://urban.hunter.cuny.edu/%7Econning/papers.html>* (see also 19 below).
 14. Banerjee et. al., Ch 6 (credit coops) in B&U I.*
 15. Conning and Udry, “Rural Financial Markets in Developing Countries,” http://urban.hunter.cuny.edu/%7Econning/papers/Rural_Finance.pdf, see also “Why Isn’t There More Financial Intermediation in Developing Countries?,” at <http://ideas.repec.org/p/htr/hcecon/214.html> * (look at the list of downloadable references!) and other papers at <http://urban.hunter.cuny.edu/%7Econning/papers.html>*
 16. Besley, “Savings, Credit, and Insurance,” Handbook, ch 36 or “How do Market Failures Justify Interventions in Rural Credit Markets,” World Bank Research Observer 9, 1 (1995).*
 17. Gertler and Gruber, Insuring Consumption against Illness, *AER*, 3/20*
 18. Townsend, ch 9 in B&U II.
 19. Morduch, J. (1999), “The Microfinance Promise,” JEL, 37(4), 1569-1614.
 20. Banerjee, Gertler, Ghatak (2002), “Empowerment and Efficiency: Tenancy Reform in West Bengal,” *JPE*. 110, 239-280; see also Ghatak’s CV at <http://sticerd.lse.ac.uk/dps/adds/ghatak/cv-lse-sept02.pdf>
 21. Mookherjee: 8, 10, 12, 15, 16.
 22. Research topics
 - a) 1st-best: formalize Ricardian land-quality, derive implications for family-farm size, and prove that rent/yield increases more than enough to compensate for smaller farm size.
 - b) 2nd-best:
 1. Formalize U-shaped AC curve based on indivisibilities and economies of family supervision.
 2. Develop formal theory to replace four quadrant agency approach (see appendix to nature of ag firm and R’set/Lee critique of Evenson’s labor supervision paper, available on request)

IV. Development Microeconomics III: Specialization, Intensification, and the Evolution of Markets

- A. Yang, *Development Economics* (introduction by Sachs), esp chs 1,3, 9, 14.
- B. See also Sachs, Yang, and Zhang, Globalization, Dual Economy, and Economic Development; “Endogenous Transaction Costs and Division of

- Labor” and other papers on agglomeration economies, division of labor, specialization, exogenous vs. endogenous comp. advantage at <http://community.buseco.monash.edu.au/inframarginal/>)*
- C. Roumasset et. al., “Specialization and Coevolution of Agricultural Mkts.,” www.iris.umd.edu/publications/detail.asp?ID=wp&number=165 (see also “The Microeconomics of Agricultural Development in the Philippines,” UH WP 02-10, especially discussion of figures 3 and 4).
 - D. Foley, Stabilization of human population through increasing returns, *Economics Letters* 68 (2000) 309-317*
 - E. Day, The Rise and Fall of Manorialism*
 - F. James and R’set, “How to Facilitate or Stifle Economic Development: The Role of Agriculture in Indonesia and the Philippines,” *Southeast Asian Journal of Agricultural Economics*, Vol. 1, No. 2, (December 1992)*
 - G. World Dev Report, 2001/2002: Building Institutions for Markets*
 - H. North, “The New Institutional Economics and Development” and “Transaction Costs Through Time” <http://ideas.repec.org/e/pno11.html>
 - I. Kaiser&R’set, Coasean Econ and the Evolution of Marine Property http://www.economics.hawaii.edu/research/seminars/03-04/04_16_04.pdf
 - J. Research topics: combine A and C; do same for evolution of financial mkt.

V. Poverty-alleviation policies

- A. Lipton, M. and Ravallion, M. (1995), from *Handbook IIB**
- B. Lipton, “Pro-Poor Growth: the Renewed War on Poverty,” May, 2001, or Eastwood and Lipton http://www.adb.org/Documents/Periodicals/ADR/ADR_Vol_18_2.pdf
- C. http://poverty.worldbank.org/files/15174_Ravallion_PPG_Primer.pdf*
- D. Ray, ch. 7&8*
- E. *World Dev. Report*, 2000/2001: Attacking Poverty, chs. 1-5, 8*
- F. Fabella, R., ch. 4 in Balisacan, Arsenio and Shigeaki Fujisaki, eds. *Causes of Poverty: Myths, Facts and Policies: A Philippine Study*, U. of the Philippines Press;* and Roumasset, review of same, *APEL* 5/2001.
- G. B&U, ch. 11.*
- H. R’set, “The Role of Agriculture in Pro-Poor Development: A Philippine Perspective” (see also “A New Institutional Approach to Pro-Poor Agricultural Development,” esp. “Stop, Push, Facilitate”).
- I. Conning on safety nets, <http://urban.hunter.cuny.edu/%7Econning/papers/CBT.pdf> , see also <http://urban.hunter.cuny.edu/%7Econning/papers.html> *

VI. Sustainable growth and development

- A. Weitzman, in *QJE*, 1976, 65-94*
- B. Endress, Roumasset, and Tzou, A Koopmans approach to sustainable development (<http://www2.soc.hawaii.edu/econ/workingpapers/WP%2002-4.pdf>) or Sustainable Growth w/o Constraints (<http://www2.soc.hawaii.edu/econ/workingpapers/009abstract.html>)
- C. Endress and Roumasset, *J. of the Asia Pacific Economy*

- D. Dasgupta, & Maler (1993), "Poverty, Institutions, and the Environmental-Resource Base," *Hndbk, Vol. 3**
- E. B&U, ch. 13*
- F. Rset, review of Opschoor, J(Hans). B., Kenneth Button, and Peter Nijkamp, eds. Environmental Economics and Development, *American Journal of Agricultural Economics*, Aug. 2001, 796-799.
- G. Krautkraemer, J., (1994), "Population growth, soil fertility, and agricultural intensification," *J. Dev. Econ.*, 44, 403-428.*
- H. Pender, "Population growth, ag intensification, induced innovation, and sustainability: an application of neoclassical growth theory," *Ag Econ* 19; (1998); "Rural population growth, ag change and natural resource management in dev countries: Honduras,"*
- I. *World Dev Report*, 2003, selected chapters*
- J. Research topic: Combine B and G

VII. (1st) Second-Best Policy Analysis

- A. Benefit cost analysis
- B. Applied general equilibrium approaches to policy analysis
- C. Infrastructure and pricing policies
- D. Spatial and Temporal Consequences of Intervention
- E. Research topics: Replicate F5 or F6
- F. Homework: Rashid et al. (2005) conclude that there is no longer a case for parastatals in Asia. Was there ever a good case? (two pages plus diagrams/references).
- F. Readings
 1. Squire, L. (1989), "Project Evaluation in Theory and Practice," in Chenery and Srinivasan (eds), *Handbook of Development Economics Vol II*, Amsterdam, North-Holland.*
 2. Roumasset, J. and Setboonsarng, S. (1988), "Second-Best Agricultural Policy: Getting the Price of Thai Rice Right," *Journal of Development Economics*, Vol. 28, pp. 323-340.
 3. Clarete, R. and Roumasset, J. (1987), "A Shoven-Whalley Model of a Small Open Economy," *Journal of Public Economics*, Vol. 32, pp. 247-261.
 4. Clarete, R. and Roumasset, J. (1990), "The Relative Welfare Cost of Industrial and Agricultural Policy Distortions: A Philippine Illustration," *Oxford Economic Papers*, Vol. 42, pp. 462-472*
 5. Fujimura, M., Roumasset, J. and Russo (1995), "Shadow Exchange Rates, Conversion Factors, and the Equivalent Variation Foundations of Project Evaluation"*
 6. Kratz and Roumasset, "Trade Diversion, Excess Storage, and State-Trading Enterprises: Rice Policy in the Philippines," (pdf, 2000)*
 7. Rashid et al. (2005), "Grain Parastatals in Asia: Why Do they Have to Change Now?" <http://www.ifpri.org/divs/mtid/dp/mtidp80.htm>
 8. "Microeconomics of Ag Dev in the Philippines," section 3.
 9. Galiani et al., (2005), "Water for Life: the Impact of Privatization of Water Services on Child Mortality," *JPE*.

VIII. Trade Promotion, Asian Miracles/Debacles, Globalization, and 3rd best policy reform

- A. Ray, chs. 16-18*
- B. Rodrik, D. (1995), "Trade and Industrial Policy Reform," *Handbook* and/or "Paradoxes of the successful state" *European Econ Rev* 41 (1997) 411-442*
- C. World Bank, *East-Asian Miracle*, 1993*
- D. Krugman, "The Myth of Asia's Miracle," *Foreign Affairs*, Nov/Dec, 1994*
- E. Stiglitz and Yusuf, ch. 13, revisit IIC above.
- F. Roumasset, Ch. 1 in Roumasset and Barr, *The Economics of Cooperation: East Asian Development and the Case for Pro-Market Intervention*, 1992.
- G. Harley, "A Review of O'Rourke and Williamson's *Globalization and History*," *JEL*, 12/00 or review of three Williamson papers in *The Economist*, 4/20/96.*
- H. Power, "Role of Protection...", *EAER*, 6/72
- H. Roumasset, "The Political Economy of Corruption"
- I. Excerpts from Dixit and Laffont*
- J. Balisacan&R'set* and B&O, ch. 11
- K. World Dev Report 2002, chs. 5&7*
- L. Easterly, *Quest for Econ Growth*, ch on econ of scale, matching, and circles*
- M. Park et. al., "In Search of a New East Asian Development Paradigm: Governance, Markets and Institutions"*
<http://www.fondad.org/publications/diversity/Fondad-Diversity-Chapter12.pdf>
- N. R'set, "Blackhole Security," WP 00-5
<http://www.economics.hawaii.edu/research/workingpapers/005abstract.html>,
summary and blackhole diagrams available in WP 02-10, at
http://www.economics.hawaii.edu/research/workingpapers/WP_02-10.pdf
- O. Research topic: combine I and J.

Partial list of topics

Jan 10: Begin market failure, govt. failure and the role of govt. in econ dev (theorems 1-5, justice, three levels of abstraction, positive and normative, tech and pec externalities). Coasean paradigm of economic development. Homework: prove CE satisfies $MRS = MRT$ for $2 \times 2 \times 2$.

Jan 12: Collect homework; continue market failure and the role of govt.

Jan 17: Collect homework on role of welfare economics in development policy. Theorems 1b, 4.

Jan 19: Collect h'work on 4a. Theorem 3a/b and Coasean Development Economics

Jan 24-26: Collect h'work on thm 3a. Cheung as *disciple extraordinaire*. Three levels of abstraction, positive and normative, tech and pec externalities). Neoclassical, modernism, post-modernism; Critiques of SWF (Arrow, no consensus, premature sacrifice of efficiency without doing LE for basic needs, unnecessary fear of scarcity). Alternatives (new-new welfare econ; Aristotle/Wicksell). Krugman (history, methodology, Murphy). Stiglitz; dynamic pecuniary externalities; coordination of interdependent investments (farmer/trucker puzzle). Lucas on productivity miracles.⁴

⁴ "Lucas (1993) applies LBD to the question of aggregate economic growth and development (it is largely inspired by earlier work by Nancy Stokey and Alwyn Young). Krugman's paper is a series of mini essays illustrating how learning by doing can cause temporary policies to have permanent consequences."

Jan 31: History of thought ala Power, Murphy, Krugman. Supply and demand sides of coordination. Role of competition. The Facilitation-Corruption frontier. Wedge model.

Feb 2: Rice and Risk (chapter 3 in Behavior and Organization).

Feb 7-16: B&O, chs 4-7. Non-spreadability of idiosyncratic risk aversion; good (exogenous policy), bad (tractor regressions), and ugly (“sheep eating men”) of consequences and induced innovation to the rescue;

Feb 21: Mookherjee, ch 12; and B&O, ch 8-9.

Feb 23: B&O ch 10-11. Mookerjee 8, 10.

Feb 28: Geri on credit (Mookherjee and Ray: 11, 15, 16).

March 2: Finish III. Student talks on Townsend (9 in B&U II), Banerjee (2002 on tenancy), Conning-Udry (Rural Finance), and Morduch (JEL, '99).

March 7: Midterm on I-III.

March 9-23: IV-V.

April 4-27; May 3: VI-VIII.