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A Defence of Development Economics

University College of Swansea

A DEFENCE OF DEVELOPMENT ECONOMICS

INAUGURAL LECTURE

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Coming to this fine old sea town of Swansea in the centenary year of the publication of "Treasure Island", I have frequently been reminded of the fate of Captain Billy Bones. Captain Bones, laid up at the Admiral Benbow Inn, knew that, sooner or later, Blind Pew would tap-tap his menacing way up to the stairs of the inn to pass him the black spot. I, having been newly appointed to a Chair in "Development Policy and Planning" also had a shrewd idea that, before very long, one of my old ship mates would pop up to announce the abolition of my chosen area of study-development economics. Thus, when last April the College asked what the subject of my lecture tonight would be, the title "A Defence of Development Economics" seemed to be the only appropriate one. And so it has proved.[1] In August last year, accompanied by the tap-tap-tapping of a "Times" journalist typing flattering articles[2], Blind Pew materialized in the form of Dr. Deepak Lal, of University College, London. His black spot was a hundred and twenty page Institute of Economic Affairs pamphlet, entitled cunningly, "The Poverty of Development Economics" (Lal, 1982). Its final conclusion was damning: it was "that the demise of development economics is likely to be conducive to the health of both the economics and the economies of developing countries" (ibid : 109).

This death sentence of a discipline is based on the judgement that development economists as a group subscribe to a set of general propositions which Lal calls "the <u>Dirigiste</u> dogma". The <u>dirigiste</u> dogma is then defined as the beliefs that the price mechanism should be <u>supplanted</u> (and not just supplemented); that the gains in efficiency from improved allocation of given resources are quantitatively small; that the case for free trade is not valid in developing countries and that government controls on wages, prices, imports and the distribution of productive assets are necessary for the relief of

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Some of the ideas in this lecture were first expounded at a seminar at the Institute of Development Studies, University of Sussex on November 2, 1983. I wish to acknowledge gratefully the helpful comments of participants in this seminar, particularly those of Christopher Colclough, Philip Daniel, David Evans, Mike Faber and Carlos Fortin. Janet Toye also commented helpfully. Remaining failures of analysis or judgement are the author's sole responsibility.

poverty in development countries. Development economists are further charged with attempting to sustain these beliefs by the invention of a set of theoretical curiosities, that is, perversions of standard economic principles, which are held to be applicable in developing countries only. They are perversions, Lal argues, because they falsely deny the universality of rational economic behaviour and the existence of marginal substitution possibilities, on which standard economic theory relies for its familiar results.

The overarching argument is substantiated in two main ways. The first is to attempt to refute selected examples of the "theoretical curiosities" which individual development economists have produced. These range over the subjects of trade, commodities, foreign capital, industrialization and planning for redistribution with growth[3]. The second is to draw an empirical contrast between India, as a case study of the bad effects of dirigiste economic policy, and the newly industrialised countries, particularly South Korea, as a case study of countries of the economic progress that can be achieved by appropriate economic policies - free trade, care for microeconomic efficiency and the absence of government controls. The link between these two is the assertion that it is the analytical failures of dirigiste development economists which have produced the indifferent economic performance of countries which have seen so foolish as to heed their advice.

II

Some of the recent attacks on development economics have been so wrong-headed and so intellectually flimsy, that no ground needs to be given to them. Lord Bauer's recent broadsides fall into that category[4], but Lal's strictures do not. They contain some elements of truth and a satisfactory defence must start by recognising them.

The charge of inventing theoretical curiosities has enough accuracy to make one uncomfortable in rebutting it completely. The work of Professor Gunnor Myrdal, on development planning in Asia, was not entirely free from what one reviewer called a "show of iconoclasm".[5] Under a self-imposed pressure for radical intellectual originality, genuine insights are sometimes expanded into formal

theories which, on a more sustained examination turn out to be partial or entirely defective. Myrdal for example, saw that certain forms of consumption in developing countries promoted economic growth, but followed this up with the quite erroneous claim that the existence of this type of "productive consumption" proved that the standard macro-economic distinction between consumption and investment was worthless for policy-making purposes in developing countries. Other examples could be given of useful perceptions being inflated to bursting point.

It would also be hard to deny completely that some development economists have favoured the idea that the analysis of developing countries requires its own separate and distinct form of economic theory. This can be seen both in the response of structuralist economists to neo-classical positions, where the latter are held to be suitable for developed economies, but not for the special circumstances of developing countries; and, in the Marxist tradition, where the theory of capitalism is sometimes held to be relevant for advanced capitalism and the theory of imperialism relevant for countries in which capitalism is still taking root. Such crude forms of theoretical dualism are hard to defend, if only because the distinction between developed and developing economies is multidimensional and one of degree rather than one of kind. Thus, the search for a more unified theory is to be welcomed in principle.

From this it follows that certain specific pieces of theory which are said to apply to developing countries qua developing countries are indeed suspect. These include the theory that their terms of trade must undergo a secular decline; that their balances of payments are governed by a foreign exchange constraint which no form of domestic policy can ease; and the inflow of foreign finance adds to consumption, but not investment. These specific pieces of theory have, in fact, been controversial right from the point of publication, and they have not succeeded in establishing themselves either theoretically or empirically as time and debate has proceeded. This does not imply that developing countries do not face severe adverse swings in their terms of trade - commodity producers have experienced this with a vengeance in the current recession. Nor does it imply that they do not face very severe balance of payments crises - of course they do. It merely implies that these are matters which can be analysed without resort to a special kind of theory which applies only in developing countries.

Lastly, there is truth in Lal's critique of government controls in many developing countries. The elaborate work that was done by the OECD in the early 1970s is clear evidence that there are certainly around the world many examples of government intervention and regulation which do not make sense in terms of the government's own objectives. Often a government could have achieved whatever objective it was striving for in a much less cumbersome and costly way from the one which was actually chosen. This is borne out by some work done in C.D.S. in the last few months on the Indian Industrial Licensing system.[6] In the light of the evidence, it is hardly worth disputing that many developing countries do exhibit irrational forms of government intervention.

III

To have to concede all the points should not induce in development economists collectively the sudden seizure of fear and despair which carried off old Captain Bones. They do not add up to the symptoms of a subject in its death throes. This is because the elements of truth in Lal's criticisms have very different implications from those that he attributes to them.

The very notion of theoretical "curiosities" or "perversions" itself deserves further comment. It pre-supposes the existence of some body of "normal" or "correct" theory. As a mere matter of historical fact, fundamental economic theory has been constantly in dispute, economists being notoriously "people who take in each other's definitions for mangling".[7] Those belonging to Lal's school of thought have sought to entrench their particular form of economics (utilitarian marginalism) as an integral part of rationality itself. One of the devices for doing this is to insist on great selectivity in confronting empirical evidence (Toye, 1976(b):442). This results in what might be called, by extension, empirical curiosities.

There is certainly no lack of orthodox economists willing to propose theoretically well specified models, whose predictions are comprehensively out of line with all that is known about the nature of contemporary poverty in developing countries. Just to come back briefly to the earlier example of the idea "productive consumption", it has been the centre-piece of the efficiency wage hypothesis by Professors Bliss and Stern. This predicts that landlords who are monopoly buyers of labour will allow for the effects of productive consumption when setting wage rates. Thus, far from exploiting the labour whose fate they control, they will actually pay higher wages than would prevail under perfectly competitive conditions. Orthodox economists themselves have given us plentiful opportunities to contrast ugly facts with fancy models (Griffin; 1978 : 138-141).

Even if orthodox economics can be, at best, more serviceable than some development economists have seen prepared to admit, it will never be so as long as economists apply it to policy problems superficially or mechanically. Unfortunately, at present, it is precisely this superficial or mechanical application which is taken as the touchstone of ideological soundness. How often in recent years have we heard that there must be no artificial impediment to price adjustments which clear markets; that the wages of labour are no different from the price of oranges? This fashionable style of applied economics is now proposed to be extended to developing countries, when surely its inappropriateness to developed countries is already sufficiently obvious. The fact is that one does not have to be mesmerized by any dirigiste dogma to see the ill consequences of unregulated markets in developed countries. The Deputy Governor of the Bank of England, for example, who can hardly be convicted as a dirigiste under Lal's definition, has claimed that:

> "the recent exchange rate swings have played a significant part in hampering economic performance and impairing the strength of the present recovery".

He concludes that "official indifference towards exchange rate movements may tend to produce anarchy: and that benign neglect does not have benign results, but may rather result in disorder" ("Guardian").

The reason for the Deputy Governor's conclusion is not that he does not understand differential calculus and the theorems of welfare economics.[8] Rather, he has observed the domination of the foreign exchange markets by short-run operators whose main concern is to anticipate correctly the transactions of other operators. Their presence in the market gives it an intrinsic instability which frustrates the emergence of a long-run equilibrium. Generalizing from this example, it is evident that one cannot come to conclusions about economic forecasts or desirable policies in developed countries, without first being extremely well-informed about the specific context, the institutional particularities and the real imperfections of the markets under study. This is equally true for the economics of developing countries, where, additionally, the institutional particularities may be much less immediately visible to the untrained eye.

It is the skill of applying general economic principles to the intricacies of particular real contexts which development economists exercise. Since the agriculture, industry, labour, public finance and trade of developing countries often have unusual, or even unique, features, standard theorems cannot be applied automatically and wholesale. Their application requires specialist knowledge of both the inflexibilities and the sometimes surprising flexibilities which characterize individual markets. The simple postulates of economic rationality and the possibility of substitution do not, at a stroke, sweep away this requirement, which is the raison d'etre of the development economist. The only way to do so would be to hold that, unlike developed economies, developing ones have no unusual features - no short-term speculators in foodgrain markets, perhaps. Apart from being incredible, this is a special theory about developing countries of the kind that is rightly objected to.

The acknowledgement that has been made of the evidence of irrational government intervention in developing economies likewise fails to dispose of "dirigisme". A dictionary definition of dirigisme is the attempt to shape economies into rationally pre-selected forms. Thus, the fact that governments have sometimes made foolish interventions does not exclude the possibility of wise ones, or prove that all government policies are ipso facto counter-productive. If the criticism is of irrationality, or of dogmatic dirigisme, who could dissent? But if it is of dirigisme as such, it is very much less compelling. Indeed, what is being argued for by the critics of development economics is actually an alternative form of dirigisme, the dirigisme of applied welfare economies. What remains to be seen is how practical a proposition this alternative, allegedly non-dogmatic, dirigisme is.

IV

To the extent that "the counter-revolution in development theory" has a policy programme, it is the enthronement of applied welfare economics. The technique of second-best welfare comparisons is brought forward as the sole intellectual apparatus that should guide economic policy in developing countries. This is to be the new form of dirigisme, rational and non-dogmatic in character. What does this imply, and is it a practical alternative?

Let me comment first on the theoretical implications. Applied welfare economics for developing countries has been formulated in the last fifteen years as social cost/benefit analysis, by Little and Mirrlees and others (Little and Mirrlees, 1974). This form of analysis grew out of the insight that the value of an investment project which could earn or save foreign exchange was independent of any particular pattern of domestic consumption (because the foreign exchange earned or saved could be transformed by trade into consumption of any type). But it was then found that a project's value could not be established without knowledge of various other parameters which should influence the government's choice between consumption and investment. The response to this discovery was to recommend the most extensive possible use of social cost/benefit analysis throughout the economy of the developing country. Only the most extensive use of the technique could throw up the information required to break through the logical impasse that one cannot specify a discount rate for projects until one can specify a corrected or "shadow" wage rate for the unskilled labour used by the project and vice versa.[9]

That immediately raises the practical implications of the rational dirigisme of applied welfare economics. What began as a method of valuing certain types of project in isolation from the rest of the economy, thus side-stepping all the alleged dogma of macroeconomic development planning, was transformed under the pressure of its own internal logic, into an alternative method of comprehensive planning. It has had to claim sovereignty not only over public sector investment, but also over private sector investment; not only over tradeable production, but also over non-tradeable production (Little and Mirrlees, 1974 : 162-9, 192-203). In practical terms, the economic administration that would be required for this purpose would be no less large and pervasive than exists at present, and much more economically sophisticated. If one is stressing "government failure" to set against the evidence of "market failure", these requirements look so ambitious as to be self-defeating.

But leaving that aside, there is a more serious problem. Government investment policy centres around decisions affecting non-tradeable production; public capital expenditure on the social sector (buildings and equipment for education, health services, personal social services), infra-structure (water supply, sewers, roads, buses, railways, power stations) and internal and external defence (police stations, prisons, military, naval and air installations and equipment). The problem is that applied welfare economics does not have a method which is correct even in principle for estimating the value of non-tradeable output in an economy where prices are distorted and where the distribution of income is not initially optimal. So, even apart from the practicalities of administration, a comprehensive application of social cost/benefit analysis in developing countries is not possible, (Toye, 1976(a); Irvin, 1978: 104; Allen and Hinchcliffe, 1982 : 118).

Thus the counter-revolution in development theory itself exhibits the distressing tendency of theorising its insights to destruction. It started from the quite valid perception that micro-economic allocation problems were unduly neglected in developing countries. It quickly moved to the assertion that micro-economic techniques can, pushed far enough, substitute for macro-economic development planning. Now that the misleading nature

of that assertion has become apparent, the latest response is to revise the terms of the original problem. Specifically, the distortions in income distribution and in the price of labour are now to be magically spirited away.

How is this to be done? The absence of an optimal income distribution in developing countries is still to be formally acknowledged. But the desirability of correcting this situation is to be denied, in the fair name of liberty. The argument here is that "we cannot... identify equity and efficiency as the sole ends of social welfare... (o)ther ends such as 'liberty' are also valued ... (and) if redistribution entails costs in terms of other social ends which are equally valued, it would be foolish to disregard them and concentrate solely on the strictly 'economic' ends" (Lal, 1983 : 89). This argument would carry more weight if it did not imply that no liberty is ever worth trading however great the welfare gains that accrue when redistributive policies are undertaken. It would also carry more weight if it did not appear side by side with a strong desire for "a courageous, ruthless and perhaps undemocratic government... to ride roughshod over ... newly-created special interest groups" in developing countries (ibid : 33). This particular juxtaposition of political beliefs reveals the stated objection to redistribution as the tactic of classical counter-revolution: first turn libery against equality and fraternity, then overthrow liberty itself.

The distortions in the price of developing countries' labour are made to vanish by an attack on Sir Arthur Lewis' famous theory of economic development with unlimited supplies of labour (Lewis, 1954). The model is said to imply a perverse preference between income and leisure of rural workers, and to be contradicted by empirical evidence of upward-sloping supply of labour schedules in India (Lal, 1983 : 90-1). The first objection is confused. Whenever the average exceeds the marginal product of rural labour, the transfer of a worker from the subsistence to the capitalist sector allows the income of the remaining subsistence workers to rise. In the short run, everyone benefits from increased income, even without assuming backward remittances from the capitalist sector. Thus no perverse preferences among non-migrants are implied. Lewis' point is that the initial gap between capitalist and subsistence sector rewards is so large, and that population pressure in the subsistence sector is so severe, that it will be many years before capitalist sector wages are forced upwards by lack of willing migrants.[10] This seems often to be the case. India, for example, has exhibited near-constant real wages in the organized sector during a longish period of capitalist growth (Toye, 1981 : 217-8). Theoretically, upward-sloping short run labour-supply schedules in rural wage labour markets are not incompatible with this state of affairs.

If distortions in income distribution and the price of labour in developing countries obstinately refuse to disappear: and if applied welfare economics provides only an incomplete method of correcting for them in the direction of economic development, what is to be done? Either economic events can be left to take their own course, or governments must have recourse again to familiar techniques of macro-economic planning to establish the overall framework within which micro-economic choices can be rationally made. In re-asserting this conventional wisdom, it is evident that powerful ideological currents can make the obvious sound distinctly heretical. But if it is now the fashion to claim that, although price distortions are endemic in developing countries, the labour market, alone among markets, is functioning competitively, then the appearance of heresy is something worth risking. The development economist must avoid making macro-economic technique substitute for micro-economic. But equally, the substitution of micro-economic for macro-economic is not possible. Although both type of techniques are inherently limited, they can and should be used concordantly. (cf. Toye, 1983 (b), p.738).

V

Perhaps at this stage if would be helpful if I gave a summary. The story so far is that Blind Pew (alias Deepak Lal), having delivered the black spot, has just fallen under the hooves of the on-coming horses. But we must now open the mysterious oilskin packet, and, having done so, try to decipher the map which it contains. As I make it out, development economists must locate themselves by four bearings - economic behaviour, technology, institutions and politics (Sen, 1975 : 109).

The stress of the counter-revolution in development theory lies almost entirely on the first of these four. As has already been argued, rational economic behaviour is as good a working hypothesis in developing countries as it is in developed countries. Only two brief qualifications need be made here. Rationality should not necessarily be interpreted as simple profit maximation. In the presence of risk and uncertainty and high costs of information, it may be rational to adopt more complex economic objectives.[11] Also, there <u>may</u> be some cultural influences on economic behaviour, which under tuition from anthropologists or sociologists, the development economist can incorporate into his analysis. It is, however, easy to be misled into exaggerating the importance of such influences on the longer-term prospects for economic development.[12]

By contrast, the counter-revolution has very little to say about technology, institutions and politics. One of the strongest reasons for resisting the attempt to re-absorb development economics into economics pure and simple is the relatively meagre contribution which economists have made to understanding the process of technological change, in comparison with economic historians, industrial archaeologists and applied scientists themselves. Yet understanding technological change is central to understanding how development both comes about, and fails to come about. To concentrate attention on problems of resource allocation with a technology assumed to be constant; to represent technological change as an outward shift of a production possibility curve, a shift which is itself either not explained or else taken to be merely a response to changes in relative prices; to conceive of technology abstractly as an amorphous means of transforming inputs into outputs: all of these mental habits of orthodox economists treat technology as a black box, and encourage the belief that understanding it is someone else's problem.

The time when this was adequate or appropriate has long since passed. The process of technological change has for many years been the means by which global inequalities in wealth and power have been continuously re-created. The practice of technological innovation, that is the repeated application of new scientific results to the spheres of warfare, communication and production has created a world order of unequal wealth and power. Moreover, it tends to reproduce these inequalities, despite, indeed because of, constant dynamic change. This view is perhaps better grasped if it is contrasted with some simpler theories of wealth and poverty on a world scale. It does not imply that poor countries are stagnant and unchanging while rich countries make their fortunes. Nor is it a theory of infinite polarization, in which rich countries prosper precisely because they impoverish poor countries. The proposition is that dynamic technical progress, affecting rich and poor countries alike, has been historically consistent with constant relative positions, at least between groups of countries, on the scales of wealth and power.

How does this work at the global level? The key is to be found in research and development effort. R and D is that form of investment which reduces the stochastic element in innovation, quickening its pace while controlling its direction. The overwhelming bulk of R and D expenditure is made by developed countries, and it can have important detrimental affects on the economies of countries that are at a less advanced point in their development. The most important such impact is in reducing world demand for products in whose production many less advanced economies specialize, by the invention of even new and better synthetic substitutes for products such as sugar, cotton, jute, rubber and the non-ferrous metals, especially tin and copper. Although low-cost synthetics may benefit consumers in poor countries, the net impact is likely to be negative, and, if positive, will be much less than the gains derived by developed countries (Griffin; 1978 : 16).

Since the rewards of the employment of new technology will usually contain an element of monopoly rent, it is not surprising that scarce factors of production like capital and skilled labour will, contrary to the expectations of orthodox economists, tend to be drawn towards areas where they are already relatively abundant. The equilibrating flows of capital and skills towards areas of relative scarcity are dominated by larger counter-flows, as successive waves of innovation generate a continuous dynamic disequilibrium.

These influences are quite separate from the problem which has often been noted, that innovation is progressively ever more

labour-saving and capital-intensive. The plant designs that are available for adoption in developing countries are designed almost exclusively for the economic conditions of prosperous countries, and are thus highly inappropriate for the factor endowments of labour-abundant economies. Attempts to employ more labour in capital-intensive plants usually leads only to gross over-manning, which undermines the competitive position of the developing country producers who resort to it.

The continuous re-creation of global inequality via technological innovation can only be understood by examining how particular technologies change. An example to illustrate the process involved can be taken from very close to home, the metal industries, with which South Wales and Swansea itself is very familiar. Innovation undermines the demand for the products of these industries in a wide variety of different ways. It permits the substitution of alternative materials in existing end-uses of metals, glass optic fibres for copper coaxial telephone cables, printed circuits for conventional electric circuits. It abolishes some end-uses altogether, such as lead type-face, which has virtually disappeared as the printing industry has turned to computer-based technology. In still other end-uses, design improvements reduce the quantity of metal required. Wire is drawn more thinly, the thickness of metal coating is reduced without any loss of performance characteristics. In all these ways, world demand for metals is reduced, and each additional increment to world production is accompanied by an ever smaller increment to metals demand (Toye, 1983 (c); 3-14). The situation is worse than this, however. Of the world's total consumption of metals, only part comes from new primary production. The remainder comes from recycling old metal, and innovations can have the effect of increasing the proportion of recycled metal to the total produced, as when the electric arc furnace supersedes the basic oxygen process in steel-making or when "reverse vending machines" reduce the collection costs of old aluminium can stock (Chandler, 1983 : 31, 35).

It seems clear, therefore, that technological innovation in developed countries has the power to dim the prospects of industrialization drives in developing countries, at least to the extent that they are based on the mining and metals fabrication industries.

The mere relocation of industrial capacity from Swansea to Latin America and Asia does not unfreeze the existing unequal structure of wealth and power. The undoubted fact that the old multi-national companies which dominated these industries have lost much of their market control does not unfreeze it. The loss of capacity here yesterday in copper and nickel and perhaps in titanium and aluminium tomorrow, has been, and will be, counter-balanced by the acquisition of the next generation of technology, which both undermines the profitability of the previous one, and on its own expected profitability, attracts scarce resources of capital and skill.

The purpose of pointing to the relative constancy of international inequality, despite the rapid pace of industrial re-structuring, is to counter much wishful thinking that a "third world" is about to disappear. If the above analysis is right, that will not happen, for many decades to come. There is more room for optimism, however, about the possibilities of eroding absolute poverty, than of eroding global inequality. This will not be either an easy or a uniform process, and rising average standards will probably be accompanied by no progress or even immiserisation in particular countries or regions, particularly in Africa and South Asia. But some success is probable and where it is achieved, one crucial cause will be the ability to forecast correctly the economic and social consequences of given technological developments. The distribution of the gains and losses of the "green revolution" in Indian agriculture, it may be noted, was heavily determined by the agronomic characteristics of the specific high-yielding varieties of wheat which were available for adoption, and the different methods of irrigation that could be used to meet their water requirement. The identification of economically feasible technologies which have unambiguously beneficial consequences for the poorest people in developing countries is the major practical task which development economists can perform. The economists to whom technology is a series of black boxes will be as helpful in that task as the member of the profession who, when a tin of corned beef was washed up on his desert island, said to his starving comrades : "let us assume that we have a tin opener".

VI

The identification of technical changes which benefit the poorest is very far from guaranteeing their implementation. Development economists cannot directly reduce absolute poverty, on the strength of own professional skill. Their effectiveness is always mediated by particular sets of institutions (governmental and other) and by the political conjuncture. Thus as well as understanding economic behaviour and the specificities of technologies, development economists must also be able to analyse the constraints on developmental actions which institutions and politics impose. It is naive and superficial to suppose that foolish forms of government intervention can be attributed wholly to dogma, of any form, and to make an iron link between bad policies and alleged logical mistakes of named intellectuals. If Keynes himself meant to say this, in his famous closing paragraph of the "General Theory", then Keynes was equally naive. Politicians may sometimes attempt to rationalize their policies by quoting academic names, but that is a very different matter from adopting policies because some famous academic recommended them.

If we want to analyse the determinants of economic policy and performance in India, or South Korea, or elsewhere, and not merely use them as pictures of vice and virtue in a neo-classical homily, we must dig much deeper than merely asking what academic ideas were available at that particular time and place. Very few societies are so intellectually impoverished or politically or culturally restructed that politicians have no choice between clashing academic ideas. The problem is almost always why they chose one set rather than another. This question cannot be fully answered by reference to a country's political history, and to the shared perspectives which that history has bred in those who are, or wish to become politically active. But it must contribute substantially to any answer. In India, it is absurd to believe that the post-Independence economic policy was derived from the writings in the early 1950s of a few development economists, such as Singer, Prebisch and Nurkse. By that time, the demand for a nationalistic economic policy had been a key element in the Congress' anti-British struggle for over forty years , and for a Congress government to abandon it in the moment of victory would have been politically unthinkable, whatever the contents of the economics journals. (c.f. Toye, 1981 : Ch.2). If we want to find an economist to denounce, it would have to be Friedrich List, who patented economic nationalism in the 1840s (Kitching, 1980 : Ch.6). The Indian understanding of the Soviet experience was also influential, but always secondary to the imperatives of mimetic nationalism.

Development economists, therefore, cannot make much progress in understanding economic performance, if they turn their backs on history and political sociology. Equally, without the help to be derived from these quarters they are likely to be ineffective as policy advisers. The orthodox economist is content to make his calculation of gains and losses in national welfare, consequent on particular policies, and to recommend the policy which gives the greatest net welfare gain. The recommendation is addressed to a set of "authorities" who are assumed to be concerned to act in the national interest. This again is a very naive view of politics. National politics is simply the clash of sectional interests - big business versus small, financial capital versus industrial or agricultural capital, capital as a whole versus labour, and so on, and national policies are the outcomes at any one time of such conflicts. An effective policy-maker is not someone who is capable of identifying counsels of perfection, but someone who can discern the relevant interests and the underlying causes of conflict and suggests ways in which those conflicts can be tipped towards constructive rather than destructive outcomes.

Development economists have recently been very active in trying to describe and measure the economic interests which shape the policies of advanced capitalist countries towards developing countries, and some surprising results have already come out of this (Cassea, 1982). For one thing, the interests observable in different advanced countries are markedly different, and particularly so between the United States, on the one hand, and the U.K., West Germany and Japan on the other. The links between the well-being of interest groups in the U.S. and the prosperity of developing countries are much less direct and obvious than those of the U.S.'s satellites and allies in the international capitalist system. This finding has several fascinating implications. One is that the United

States would require especially far-sighted political leadership for its constitutionally entrenched position in such international organisations as the World Bank and the I.M.F. not to impede, rather than improve the prospects for world development. Another is that the current revival of Cold War attitudes and postures helps to obscure important differences between interests in the U.S. and in Europe and Japan in the promotion of Third World development. In these circumstances, the constructive response must be to research more thoroughly the specific mutual benefits which Third World development generates, in the hope that they will achieve greater political visibility. The destructive response is simply to turn up the volume of the public praise of free markets and the public denunciation of something called "dirigisme".

VII

Thus the defence of development economics against the attempt to re-absorb it in the mainstream of orthodox economics requires the maintenance and, if possible, the strengthening of certain intellectual alliances. The need to model and evaluate specific processes of technical change implies a good working relationship between development economists and applied scientists in such fields as metallurgy, agronomy, genetics, engineering, forestry, and so on. The need to seek reforms and improvements within institutions and political communities of all kinds implies active co-operation between development economist and anthropologists, sociologists, historians and students of political processes.

In the end, development economics can be saved from the uni-disciplinary purity of the orthodox economists only by establishing it as one interdependent element in the multi-disciplinary undertaking which we call development studies. At the heart of development studies lies an intellectual commitment to find the causes of the persistence of inequality and poverty on a world-wide scale. In this quest, disciplinary boundaries between economics and other subjects cannot be regarded as sacrosanct. They must be crossed and re-crossed as the needs of the problem dictate. As scholars we must set an example of curiosity, open-mindedness and willingness to learn from colleagues trained in unfamiliar ways of thinking. This may also help us as citizens to learn to co-operate rationally with our fellows in the discharge of our deeper human obligations, to feed the hungry, to heal the sick and to make a just peace between enemies.

NOTES

1. If there is a hint of paranoia here, it could be pleaded in mitigation that delivery of an inaugural lecture can be a distressing experience. The late Professor Gallagher loved to recall the inaugural lecture given by the newly-endowed Professor of Macedonian History at the University of Nis, whose first sentence ("The Macedonian problem is one of immense complexity") was followed by the enormous bang of a terrorist bomb which blew him and his audience sky-high (Cobb, 1983). This anecdote is somewhat harder to laugh at, however, if for history we substitute development policy, and for Macedonia we substitute Lebanon, Nicaragua or even Eire.

2. The articles were under the headlines "Third World Theories Attacked" (August 22, 1983) and "Third World Theories face a Counter-revolution" (September 9, 1983). The "Times" articles see Lal's book as not merely as counter revolutionary in theory but also as likely to have substantial policy consequences. One is perforce reminded of an IEA booklet called "Money in Boom and Slump" published by Professor Alan Walters (Walters, 1969), which heralded the U.K. campaign for "monetarism" and ended with him knighted and advising the Prime Minister on the management of the British economy. So one should be wary of dismissing Lal's effort, slim though it is, as of no consequence. The policy implications which the "Times" thinks flows from it are, first a move in developing countries towards smaller government and more open economies and, second, that even less aid will be given by developed to developing countries until the policies which it advocated are adopted in those countries.

3. To be specific, Nurkse is criticized for his demand-based view that developing countries face poor prospects for their exports of primary products; Prebisch and Singer for their claim of a secular decline in terms of trade with developing countries;

Chenery and Strout for their theory of a foreign exchange constraint which no domestic policies can possibly remove; Sir Arthur Lewis is contradicted under two headings: his theory of Capitalist accumulation based on surplus labour at a constant wage rate is denied by Lal, as is his interesting theory explaining the historical origins of unequal exchange in terms of the relative productivity of temperate and tropical food producers. Griffin and Enos are criticised for their view that foreign financial inflows depress domestic saving; Frances Stewart for saying that such inflows give rise to a set of products which are inappropriate for customers in developing countries; Feldman and Mahalanobis are criticised for the view that the fastest growth strategy is one which starts by investing in the machines which make machines and, Kuznets is pilloried because he claimed that inequality of incomes rises as development takes place and then falls away. Other doctrines and other development economists are also found to be in error. But the above gives a good indication of the width of Lal's attack, if not of the depth of it.

Lal admits that he "does not imply that all those who have supplied ammunition for the <u>dirigiste</u> armoury would accept the purpose for which it has been deployed." Nor does he "outline the various qualifications these economists rightly made in putting forward (their) ideas ..." (Lal, 1983 : 2). In some instances, however, the Lal's lapses of scholarship amount to much more than the omission of qualifications to an argument, and constitute a complete mis-reading of a given author. Lal cites with approval Hirschman's dictum that Marx would have believed traditional economics to be equally applicable to developed and developing countries, but denied that economic relations between them could be mutually beneficial. This seems to be wrong on both counts. Marx certainly does not apply a uniform economics regardless of social structure, but distinguishes, for example between merchant capitalist exchanges and industrial capitalist exchanges. He does, however, hold that "exchange is a transaction by which both sides gain" (Marx; 1978 : 259). On the very same page, Lal cites the work of Arrighi Emmanuel as evidence of neo-Marxists' "desire to smash the whole world capitalist system based on 'unequal exchange'" (Lal, 1983 : 7), whereas in fact Emmanuel believes that capitalism is a progressive social system which is frustrated in its beneficial impact on developing countries by the mechanism of 'unequal exchange'. (I am grateful to Dr. David Evans for elucidating these points).

The fact that certain tenets of development economics have been examined and found wanting seems to be a mark in its favour, and not otherwise, as Lal would have it. It testifies to the ability of development economists as a group to be dispassionate and to sift error from provisional truth - sometimes quite quickly. If we take the example of Chenery and Strout's theory of a domestically unshiftable foreign exchange constraint, the decisive refutation was made in 1970, only four years after the theory was fully laid out, by Joshi, 1970 : 111-133. This refutation was subsequently endorsed by other development economists e.g. Griffin, 1978 : 60-1, 79, 80.

4. The reference is to Bauer, 1981. For a thorough-going rebuttal see Sen, 1982 and Toye, 1983 (a). Other reviews, all critical, include Colclough, 1982, Lipton, 1981 and Smith, 1982.

5. The reference is to Myrdal, 1968. The reviewer was Byres, 1969. See also the comments in Toye, 1981; 68-70.

6. The research referred to was undertaken by Mr. A. Nath in preparation for an M.Sc. thesis. The responsible department of the Government of India publishes information about the length of time it takes to grant clearance or permission to people who want to make industrial investments and these delays may last anything up to three years. It is a fairly simple task to calculate roughly what the cost to the investor is of delaying his investment for any given period. Apart from the length of delays, the information required is the marginal rate of return in the industry concerned and an appropriaate rate of discount. A methodology for the related problems of the impact of delays on loan-financed projects can be found in Harvey, 1983 : 71-88. The costs of delay were found to be well in excess of the direct

costs of the civil servants who operated the licensing system, and its benefits in curbing the monopolisation of industry by the so-called "large houses" were very difficult to detect.

7. Phyllis Deane has recently surveyed the methodological debates among economists in the 1870s and 1880s, in her Presidential Address to the Royal Economic Society. From that survey, she concluded:

"The lesson, it seems to me, that we should draw from the history of economic thought is that economists should resist the pressure to embrace a one-sided or restrictive consensus. There is no one kind of economic truth which holds the key to fruitful analysis of all economic problems, no pure economic theory that is immune to changes in social values or current policy problems" (Deane, 1982 : 11).

8. According to the Preface to Lal's book, by Martin Wassell, "the clergymen and other well intentioned souls who lobbied Parliament on the Brandt Report would do well --- to make more mental effort to understand the intellectual case against the Dirigiste Dogma" (Lal, 1983 : xi, emphasis in original). It is hoped that this lecture will assist them to do precisely that.

9. The problem, stated simply, is this,

(a) it is assumed that all prices, including the price of unskilled labour, in a developing economy are distorted. That is they differ, in unknown ways, from the prices that would prevail in a general equilibrium of perfectly competitive markets;

(b) the value of all the commodities used in an investment project can be derived either from prices that prevail in international markets (assumed to be perfectly competitive here for simplicity of exposition), or from the value of unskilled labour;

(c) the value of unskilled labour in an industrial project is given by the opportunity cost of its move from agriculture, which is its marginal product in agriculture (m) plus the difference between the industrial wage (c) and m (this difference being assumed to be additional consumption), this difference being weighted to reflect the social desirability, in the government's eyes, of additional consumption.

Thus shadow wage rate (SWR) = $m + (c - m)\left(1 - \frac{1}{S}\right)$

(d) So, the final term in the above equation, is approximated by the following formula:

$$S = \left(\frac{1 + r}{1 + i}\right)^{T} \left(\frac{(c - m)\,n}{r - i} + 1\right) - \frac{(c - m)\,n}{r - i}$$

where:

T is the number of years over which the government wishes to weight the choice in favour of investment rather than consumption;

n is the number of men employed per unit of investment cost;

r is the rate of re-investment of the marginal investment project;

i is rate by which future consumption is discounted.

Clearly, whereas T, u and i cause specified <u>exante</u>, r cannot, because the marginal investment project cannot itself be identified until the SWR is known. But the formula itself states that the SWR cannot be known until S, and r are themselves known. The only solution to this problem is to collect information, on <u>all</u> the available investment projects in the economy, make initial estimates of the SWR or the discount rate. If the investment cost of the chosen projects exceeds or falls short of the available supply of capital funds, the SWR and the discount rate can be adjusted together until the excess or shortfall is eliminated.

10. To the extent that the Lewis model involves difficult assumptions about preferences, in orthodox economic theory, they concern the <u>migrant</u> or person who transfers from the subsistence to the capitalist sector, not those who remain in their original sector. This has been stated as follows.

> "A movement away from one's farm may involve the loss of one's share of the family income ... what wage (the peasant) will accept as minimal compensation depends partly on the exact distribution system in the peasant set-up and partly on his concern for the welfare of the joint family as compared with his own welfare ... The greater his concern, the more willing he will be to move, since his loss of implicit rent is gain for the others in the joint family". (Sen. 1975 : 54-5 and 54n.6.)

The factual evidence of transfer is sufficient to show that <u>this</u> preference problem cannot be empirically insuperable.

11. It has been argued that poor peasants may rationally choose to avoid planting the crop combination that would maximize their profits, if that combination involved taking risks which, if their outcome was adverse, would imperil survival. See, for example, Lipton, 1968.

12. This is still disputed territory between orthodox economist and non-orthodox. Olson (1982) has recently claimed to be able to explain some significant "social rigidities" in terms of the application of orthodox economic theory. Some of the strong assumptions required by those who use rational choice theory as a source of positive explanation are brought out by Hindess (1983).

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