

# Growth and Development:

## Growth vs. Development

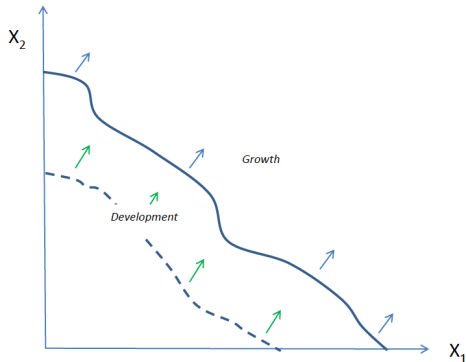
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Lecture Notes for PhD Growth and Development (EC8510)

# Growth vs. Development

- Growth focuses on fundamental parameters



- Development focuses on how two economies with the same fundamentals allocate resources differently.

# Growth vs. Development

- ▶ The Growth view:
  - ▶ Markets are complete and perfect
  - ▶ Benign social planner
  - ▶ Representative economic agent
  - ▶ Economic agents are rational
- ▶ The Development view:
  - ▶ Markets fail
  - ▶ Governments fail
  - ▶ Intra-household conflict
  - ▶ Social constraints
  - ▶ Bounded rationality/cognitive bias

## Micro Stylized Facts – Banerjee and Duflo (2007)

- ▶ Use household survey data from 13 countries to look at the lives of:
  - ▶ The extremely poor (EP): consumption  $< \$1.08$  per day per capita in '93 PPP
  - ▶ The poor: consumption  $< \$2.16$  per day in '93 PPP
- ▶ To put this in perspective the poverty line in the US is around \$13 per day.

## A Useful Exercise

- ▶ The surveys are not exhaustive or representative.
- ▶ But, a novel attempt to use household data across countries to look at the economic lives of the poor, hidden in the aggregate statistics.
- ▶ **Take-home:** There is considerable variation in living standards both within & across countries: the poor are not homogenous.

# Demographics

- ▶ **Large family size:** 6-12 members (median 7.8) vs. 2.5 in the U.S.
- ▶ **No. of adults per HH (age > 18):** 2.5-5 (median 3)
  - ▶ More than just 'husband and wife' – other adults co-habit like parents, siblings, uncles, cousins, etc.
- ▶ **Large number of children:** ratio of HH members < 18 to HH members > 51 is 3-9 in rural (median 6) and 2-11 in urban (median 6) vs. 1 in the U.S.

Why might poor households have such large households?

# Food Consumption

- ▶ **EP HHs do not spend more on buying calories, even though they can afford up to 30% more**
  - ▶ Poor and EP seem to spend the same amount on food
  - ▶ Deaton and Subramanian (1996) – 1% ↑ in total expenditures  $\Rightarrow$  0.67% ↑ total food expenditures.
- ▶ **EP do not optimize on buying edibles with the greatest nutrition per \$, e.g., millet**
  - ▶ Spend almost 7% of budget on sugar
  - ▶ For every 1% increase in food expenditure 50% = more calories and 50% = more expensive (and tastier) calories.
  - ▶ Suggests EP do have some margin of choice and choose not to exercise it in the form of buying more food



# Physical Health

- ▶ **Those in the EP category consume <1,400 calories a day.**
  - ▶ Half the recommended level of consumption for a male with moderate activity.
- ▶ Among the EP
  - ▶ 57% report that HH members had enough to eat throughout the year
  - ▶ 11-46% report having a member being either bedridden for the day or requiring a doctor in the past month

# Mental Well-Being

- ▶ Self-reported happiness or health levels not particularly low
- ▶ But poor report high levels of stress – financial and psychological
- ▶ Cutting meals strongly correlated with reported unhappiness
  - ▶ 45% of adults in EP HHs had to cut the size of their meal.
  - ▶ 12% children had to cut the size of their meal.

Why don't poor households eat more/better?

# Ownership of Productive Assets

- ▶ **Land is a major asset**

- ▶ Great variations in ownership across countries

- ▶ 4% of EP own land in Mexico vs, 85% in Panama, vs. 99% in Udaipur

- ▶ When EP own land, plots tend to be very small

- ▶ Median landholding < 3 ha.

- ▶ **EP HHs own very few other assets**

Why don't poor households expand cultivation?

# Entrepreneurship

- ▶ **Substantial fraction of the poor work as entrepreneurs**

- ▶ Raise the capital, carry out the investment, and are the full residual claimant of earnings.
- ▶ 47%+ of the urban poor operate a non-farm business
- ▶ 25-98% of the rural EP report being self-employed in agriculture
- ▶ 7-36% of the rural Poor also run a non-farm business.

**Policy Question:** Should we encourage this form of “petty” entrepreneurship, or attempt to expand formal sector employment opportunities?

# Multiple Jobs

- ▶ Up to 47% of the urban poor get income from > 1 source.
- ▶ Pattern of multiple occupations stronger in rural areas.
  - ▶ Poor cultivate own land – no more, no less. Yet agriculture is not the main source of income.
  - ▶ Also work as daily laborers – 94% of the EP report doing this; 74% claim this as the main source of income.
- ▶ Median family has 3 working members and 7 occupations

# Lack of Specialization

- ▶ Engaged in multiple occupations, in multiple locations, but do not pursue/specialize in one
- ▶ In the labor market, specialized competence that takes a long time to acquire is associated with higher earnings.
- ▶ But even non-farm businesses run by the poor do not hone specialized skills.
- ▶ In many ways, the poor trade-off opportunities to have higher income for present consumption.



# Economies of Scale

- ▶ Very small landholdings; do not rent more land; seasonal cultivation.
- ▶ Non-farm businesses also very small scale
  - ▶ The median business of the poor have close to no paid staff.
  - ▶ Operated by 1.4-2.6 people (mostly family members)
  - ▶ Few assets (most common assets are tables, scales, and pushcarts)
- ▶ Small-scale usually means efficiency gains could be had through consolidation and specialization.

Why don't poor households specialize more?

# Temporary Migration

- ▶ Temporary migration is a major source of non-farm income for the rural poor.
- ▶ 60% of rural EP HHs report that someone from the family had lived outside the home for some part of the year to obtain work.
- ▶ Multiple trips per year
- ▶ Median length of one month; only 10% of episodes > 3 months.
- ▶ 28% stay within the district. Only 42% leave the state.

# Permanent Migration

- ▶ Share of EP HHs who had one member born elsewhere and had migrated for work reasons is very low.
  - ▶ 4% in Pakistan
  - ▶ 6% in Cote D'Ivoire
  - ▶ 10% in Peru
  - ▶ 14% India
  - ▶ 41% in Indonesia (but migration is subsidized)

Why don't people migrate for longer?

# Insurance

- ▶ Very little access to formal insurance
  - ▶ 6% of EP covered by health insurance (exception is Mexico where 50% have coverage)
  - ▶ Life insurance more common in India: 4%-10%
  - ▶ Access to weather insurance is very rare in most places (changing)
  - ▶ Governments are supposed to provide free healthcare to the poor...
  - ▶ Some governments offer safety net “Food for Work” programmes

# Insurance

- ▶ Access informal insurance through social networks
  - ▶ Over 1 year,
    - ▶ 75% of poor villagers in Nigeria had made loans,
    - ▶ 65% had borrowed money,
    - ▶ 50% had been both borrowers and lenders
  - ▶ all among friends and neighbors ([Udry, 1990](#))
  - ▶ Similar protection through jati/sub-caste networks in India ([Rosenzweig and Munshi, 2016](#))
- ▶ Informal insurance provides only limited protection

# Insurance

- ▶ Poor HH consumption strongly affected by variations in income
- ▶ HHs bear health-related risks directly.
- ▶ Often the only form of insurance is eating less or taking children out of school
- ▶ Lack of insurance also leads poor to under-invest in risky, but profitable, technologies.



# Savings

- ▶ Difficult for poor to find a safe place to save money and earn reasonable returns
  - ▶ Saving at home does not protect from inflation, needy relatives and friends, and temptation to spend
- ▶ Few EP HHs have bank savings accounts
  - ▶  $< 14\%$  in sample countries (except Cote d'Ivoire = 79%)
- ▶ So poor save informally,
  - ▶ Savings clubs, chit funds, ROSCAs, credit unions, post office savings, etc.

Why don't poor households save more?

# Investment in Education

- ▶ Enrollment of children in schools is high – at least 50% of both boys and girls aged 7-12
- ▶ EP spend very little on education ( 2% of HH budget)

Why don't poor households invest more in education?

# Education and Healthcare Services

- ▶ Some attempt made to expand access in these areas
  - ▶ e.g. most Indian villages have a school within 1 km and a health sub-centre for every 10,000 people.
- ▶ However, quality of services is very low
  - ▶ Very high absenteeism by teachers (19%) and health workers (35%)
  - ▶ Competence of providers is usually low
    - ▶ Treatments suggested by the average provider more likely to do harm than good ([Das and Hammer, 2004](#))

# Education and Healthcare Services

- ▶ Poor healthcare and sanitation directly affect mortality:
  - ▶ Very large differences in survival chances of poor children across countries
- ▶ Low quality of teaching in public schools affects learning
  - ▶ In India, 93.4% of children aged 6-14 are enrolled in schools, but,
    - ▶ 35% cannot read a simple paragraph at class 2 level;
    - ▶ 41% cannot do subtraction;
    - ▶ 66% cannot do division;
  - ▶ Even among children in class 6-8, 22% cannot read a class 2 text.

# Access to Physical Infrastructure

- ▶ While poverty is measured and conceived in terms of private consumption, this is too narrow a view.
- ▶ Holding constant private consumption, quality of life very different based on access to safe water, electricity, and other public goods.
- ▶ Huge variation in access to physical infrastructure.
- ▶ Different kinds of infrastructure do not always appear together.
- ▶ Government effectiveness in delivering these services can be very low

How might we improve public service/good delivery/provision?

# Poverty Traps

- ▶ These stylized facts suggest that:
  - ▶ Poor households have high discount rates: low saving in good times.
  - ▶ The poor quality of infrastructure prevents prolonged investment and specialization in any one occupation.
  - ▶ Low ownership of physical assets + limited access to cheap capital + high aversion to risk = limited investment beyond small-scale operations.
- ▶ Low incomes persist.
- ▶ Understanding micro-foundations may help to explain the lack of convergence observed at macro level.