# Lord Bauer

P. T. BAUER was born in Budapest in 1915. He is a Fellow of the British Academy, Fellow of Gonville and Caius College, Cambridge, and was Smuts Reader in Commonwealth Studies, Cambridge University, 1956–60, and Professor of Economics (with special reference to economic development in underdeveloped countries) at the London School of Economics, 1960–83. He was raised to the peerage in 1983.

His early publications stem from field work in Malaya and West Africa. His books include *The Rubber Industry* (Cambridge, Mass.: Harvard University Press, 1948); *West African Trade* (Cambridge, Eng.: Cambridge University Press, 1954; London: Routledge and Kegan Paul, 1963); with B. S. Yamey, *The Economics of Under-developed Countries* (Chicago: University of Chicago Press, 1957); *Economic Analysis and Policy in Underdeveloped Countries* (Durham, N.C.: Duke University Press, 1957; Cambridge, Eng.: Cambridge University Press, 1958); *Indian Economic Policy and Development* (London: Allen and Unwin, 1961; Bombay: Popular Prakashan, 1965); with B. S. Yamey, *Markets, Market Control and Marketing Reform* (London: Weidenfeld and Nicolson, 1968); *Dissent on Development* (London: Weidenfeld and Nicolson, 1971; Cambridge, Mass.: Harvard University Press, 1972); *Reality and Rhetoric: Studies in the Economics of Development* (Cambridge, Mass.: Harvard University Press, 1984).

Among his articles are "The Working of Rubber Regulation," *Economic Journal*, September 1946; with B. S. Yamey, "Economic Progress and Occupational Distribution," *Economic Journal*, December 1951; with F. W. Paish, "Reduction in the Fluctuations of Incomes of Primary Producers," *Economic Journal*, December 1952; with B. S. Yamey, "East-West/North-South," *Commentary*, September 1980.

Lord Bauer has published extensively on major issues in the general field of economic development, including the role of trading activity and the significance of the informal sector in developing countries; the role of cash crops in development; the relation between economic progress and occupational distribution; conceptual and practical problems of price and income stabilization; and the operation of commodity agreements. His contributions also offer an effective critique of received opinion on such issues as the vicious circle of poverty, the widening gap of income differences within and among countries, the operation of foreign aid, and the theory and practice of development planning. He has also written on questions of methodology in economics, notably on the tendency in modern economics to ignore the interaction of variables and parameters.

# Remembrance of Studies Past: Retracing First Steps

THE FOLLOWING is a reasonable summary of the principal components to the burgeoning development literature of the early postwar years.[1]

External trade is at best ineffective for the economic advance of less developed countries (LDCs), and more often it is damaging. Instead, the advance of LDCs depends on ample supplies of capital to provide for infrastructure, for the rapid growth of manufacturing industry, and for the modernization of their economies and societies. The capital required cannot be generated in the LDCs themselves because of the inflexible and inexorable constraint of low incomes (the vicious circle of poverty and stagnation), reinforced by the international demonstration effect, and by the lack of privately profitable investment opportunities in poor countries with their inherently limited local markets. General backwardness, economic unresponsiveness, and lack of enterprise are well-nigh universal within the less developed world. Therefore, if significant economic advance is to be achieved, governments have an indispensable as well as a comprehensive role in carrying through the critical and large-scale changes necessary to break down the formidable obstacles to growth and to initiate and sustain the growth process.

These ideas became the core of mainstream academic development literature, which in turn has served as the basis for national and international policies ever since. Even when some elements of the core have disappeared from more academic writings, they have continued to dominate political and public discourse, an instance of the lingering effects of discarded ideas.

My earliest investigations of economic issues in LDCs were not inspired by these topics; in fact, they were altogether unconnected with them.[2] I

1. Detailed references to the early development literature are given in my *Dissent on Development* (London: Weidenfeld and Nicolson, 1971; and Cambridge, Mass.: Harvard University Press, 1972), passim, especially chaps. 1 and 2.

2. The results of my studies are to be found in the following publications: P. T. Bauer, *The Rubber Industry* (Cambridge, Mass.: Harvard University Press, 1948); *Report on a Visit to the Rubber-Growing Smallholdings of Malaya, July–September 1946* (London: Colonial Office, 1948); *West African Trade* (Cambridge, Eng.: Cam-

came to this general area through two studies, one of the rubber industry of Southeast Asia, and the other of the organization of trade in the former British West Africa. I spent more than ten years on these studies during the 1940s and 1950s when I was for substantial periods in each of the two regions. What I saw was starkly at variance with the components of the emerging consensus of mainstream development economics listed above. My enquiries into and observation of economic, social, and political life in these two major regions provoked a lasting interest in general development economics. Although my ideas have developed much since the completion of these studies, they have not moved closer either to the tenets of the development orthodoxy of the 1950s or to their subsequent modification.

## [1]

Even before setting foot in Southeast Asia and West Africa I knew that many of their economies had advanced rapidly (even though they were colonies!). After all, it required no instruction in development economics to know that before 1885 there was not a single rubber tree in Malaya nor a single cocoa tree in British West Africa. By the 1930s there were millions of acres under these and other export crops, the bulk of them owned and operated by non-Europeans. But while I knew this and a good deal else about local conditions, I was nevertheless surprised by much of what I saw, including the extensive economic transformation occurring in large areas and the vigor of economic life of much of the local populations. In Malaya (now Malaysia), for example, the economic activity of the many towns and large villages, the excellent communications, and the evident prosperity of large sections of the non-European population reflected a world totally different from the largely empty and economically backward Malaya of the nineteenth century. The results of somewhat similar, though less extensive, changes were evident also in West Africa, most notably in southern Nigeria and the Gold Coast (now Ghana). How was all this possible if there was any real substance in the central ideas of the contemporary development economics?

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bridge University Press, 1954; London: Routledge and Kegan Paul, 1963); *Economic Analysis and Policy in Underdeveloped Countries* (Durham, N.C.: Duke University Press, 1957; and Cambridge, Eng.: Cambridge University Press, 1958); and, with B. S. Yamey, *The Economics of Under-developed Countries* (Chicago: University of Chicago Press, 1957), and some of the essays in *Markets, Market Control and Marketing Reform* (London: Weidenfeld and Nicolson, 1968). I want to make it clear that since 1951 I have worked so closely with Basil Yamey that the ideas in this paper are his as much as mine. It is for convenience of exposition alone that I do not make the distinction in the text between our joint work and my own.

In the earliest stages local supplies of capital were minimal. In Southeast Asia, however, the export market for rubber (and to a lesser extent other products such as tin) attracted investment by European enterprises, particularly for such purposes as the development of rubber estates in hitherto empty jungle. Where local labor supplies were inadequate, as in Malaya and Sumatra, the Western enterprises organized and financed large-scale recruitment and migration of unlettered workers, mainly from China and India. The activities of the Western enterprises induced unintended and unexpected sequences. For instance, Chinese traders were drawn into the rubber trade. Some started their own plantations, while others brought seeds and consumer goods to the indigenous people of Malaya and the Netherlands Indies (now Indonesia). They thereby encouraged the local population to plant rubber trees and to produce for the market. By the late 1930s, over half of the rubber acreage of Southeast Asia was owned by Asians. This acreage represented the results of direct investment despite initially low incomes.[3]

The history was somewhat different in West Africa. In this region there were (and are) no European-owned plantations. The large area under cocoa, groundnuts, cotton, and kola nuts has been entirely occupied by farms established, owned, and operated by Africans. The extensive capital involved was made available partly by European trading firms which financed local traders, and partly by direct investment by Africans, the latter in important instances carried out by migrant farmers in regions far from their homes.

In all this the role of traders was crucial: Sir Keith Hancock has rightly called West Africa "the traders' frontier." The traders made available consumer goods and production inputs, and provided the outlets for the cash crops. Their activities stimulated investment and production. The part played by what used to be called inducement goods—a term once a household expression but now rarely encountered in modern development literature—was notable. The sequence showed the inappropriateness of the notion of the international demonstration effect, the idea that access to cheap consumer goods, especially imported goods, retards development in the LDCs by raising the propensity to consume of the local populations.

The rapid economic progress generally in these areas, of which the large-scale capital formation in agriculture by the local people was a major

3. The plantation rubber industry comprises smallholdings, that is, properties of less than a hundred acres each, and estate properties of more than a hundred acres each. Smallholdings, which account for well over half the total area, are entirely in Asian ownership. By now well over half of the estates are also in Asian, largely Chinese, ownership. In a private communication in January 1983, W. G. G. Kellett, who was for many years chief statistician of the International Rubber Regulation Committee and subsequently of the International Rubber Study Group, put the present Asian ownership at well over 90 percent.

component, cannot be squared with the idea of the vicious circle of poverty and stagnation. It would have been a freak of chance if I had happened on the only two regions in the less developed world where people had managed to escape the imperatives of a law of economics. In fact, of course, the notion of the vicious circle of poverty, that poverty is self-perpetuating, is belied by evidence throughout the developed and less developed world, and indeed by the very existence of developed countries.

The notion is not rescued by the suggestion, much canvassed since the 1950s, that the production of commodities for export resulted merely in enclaves operated by Westerners without benefit to the local people. As I have said, a large part of production, and sometimes the entire output, was (and remains) in the hands of the local population. The same applies to the associated activities of trade and transport. Had this been otherwise, the development of export crops could not have transformed the lives of the local people as it has done. In these regions, as in many others, the pervasive economic advance has made it possible for much larger populations to live longer and at much higher standards.

A developed infrastructure was not a precondition for the emergence of the major cash crops of Southeast Asia and West Africa. As has often also been the case elsewhere, the facilities known as infrastructure were developed in the course of the expansion of the economy. It is unhistorical to envisage an elaborate and expensive infrastructure as a necessary groundwork for economic advance. Countless people in trading and transport often performed the services usually associated with capital-intensive infrastructure. For instance, human and animal transport, the contacts between numerous traders, and long chains of intermediaries were partial but effective substitutes for expensive roads and communication systems.

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The historical experience I have noted (and which had its counterpart in many LDCs) was not the result of conscription of people or the forced mobilization of their resources. Nor was it the result of forcible modernization of attitudes and behavior, nor of large-scale state-sponsored industrialization, nor of any other form of big push. And it was not brought about by the achievement of political independence, or by the inculcation in the minds of the local people of the notion of national identity, or by the stirring-up of mass enthusiasm for the abstract notion of economic development, or by any other form of political or cultural revolution. It was not the result of conscious efforts at nation building (as if people were lifeless bricks, to be moved about by some master builder) or of the adoption by governments of economic development as a formal policy goal or commitment. What happened was in very large measure the result of the individual voluntary responses of millions of people to emerging or expanding opportunities created largely by external contacts and brought to their notice in a variety of ways, primarily through the operation of the market. These developments were made possible by firm but limited government, without large expenditures of public funds and without the receipt of large external subventions.

The nature of these responses in turn exposed for me the hollowness of various standard stereotypes. It was evident that the ordinary people of the LDCs were not necessarily torpid, rigidly constrained by custom and habit, economically timid, inherently myopic, and generally deficient in enterprise. In a decade or two, the illiterate peasantry of Southeast Asia and West Africa planted millions of acres under hitherto unknown cash crops, rubber and cocoa, which take five years to become productive. The large volumes of direct investment to achieve this were made possible by voluntary changes in the conduct, attitudes, and motivations of numerous individuals, in many cases involving the sacrifice of leisure and the modification of personal relationships. Yet Malays, Indonesians, and Africans were precisely among those who were depicted (as they still sometimes are) as incapable of taking a long view or of creating capital, and as being hobbled by custom and habit.

The establishment and operation of properties producing cash crops are entrepreneurial activities. So also are the ubiquitous trading and transport activities of local people. The contention is thus invalid that entrepreneurial skills and attitudes are lacking in LDCs. Indeed, they are often present but take forms which accord with people's attributes and inclinations and with local conditions and opportunities. In many parts of the less developed world there is evidence of much enterprise and risk-taking, often on a small scale individually, but by no means confined to agriculture and trading.

The contribution to economic development of the numerous small and large-scale entrepreneurs (farmers, traders, industrialists, and so on) highlights the generally melancholy record of the entrepreneurial efforts of LDC governments—all too often financed at large cost from revenues derived by taxing the producers of cash crops. It is often claimed in the development literature, in support of the alleged need for extensive state control and direction in the economies of many LDCs, that their populations lack entrepreneurs. Should the people of a particular country in fact be without entrepreneurial talents or inclinations, it is difficult to see how the politicians and civil servants from this population could make up for the deficiency.

In the less developed world, willingness to bestir oneself and to take risks in the process is not confined to entrepreneurs in the accepted sense of the term. Hundreds of thousands of extremely poor landless rural people have migrated thousands of miles to improve their lot. The large-scale migration from southeastern China and southern India to Fiji, Malaya, and the Netherlands Indies is well known. In my work I was able to show that very poor illiterate people were well informed about economic conditions in distant and alien countries, and that they responded intelligently to the opportunities they perceived.[4]

## [3]

When I began my work, the emerging ideas on economic development assigned decisive importance to the ratio between number of people on the one hand, and available resources—land and other natural resources, as well as capital—on the other. Given the size of population, physical resources were all that mattered. Apart from age and sex differences, people were envisaged as homogeneous from an economic point of view. All this can be seen in the construction of the growth models of contemporary economic literature and in the discussion these inspired. The only partial qualification was provided in the growing emphasis on human differences resulting from capital embodied in people.

My existing skepticism about this approach was soon and amply reinforced by what I saw in Southeast Asia. The differences in economic performance and hence in achievement among groups were immediately evident, indeed startling. Perhaps the clearest demonstration that people, even with the same level of education, cannot be treated as being uniform in the economic context was to be found in that region.

Many rubber estates kept records of the daily output of each tapper, and distinguished between the output of Chinese and Indian workers. The output of the Chinese was usually more than double that of the Indians, with all of them using the same simple equipment of tapping knife, latex cup, and bucket. There were similar or even wider differences between Chinese, Indian, and Malay smallholders when I visited several hundred smallholdings in Malaya in 1946. The pronounced differences between Chinese and Indians could not be attributed to the special characteristics often possessed by migrants, as both groups were recent immigrants. The great majority of both Indians and Chinese were uneducated coolies, so that the differences in their performance could not be explained in terms of differences in human capital formation. The Chinese performance in Malay was especially notable. Not only had practically all the Chinese been very poor immigrants, but also they were subject to extensive adverse discrimination imposed by the British administration and by the local Malaya rulers.

Of course, differences among groups were not limited to expertise in rubber tapping or in other aspects of rubber production. They were pervasive throughout the local economies in the establishment and run-

4. See *The Rubber Industry*, chap. 15 and app. D; and *Economic Analysis and Economic Policy*, chap. 1.

ning of plantations and mines and of industrial and commercial undertakings. These differences in no way resulted from differences in the initial capital endowments of the groups. In fact, of course, these differences meant that the various groups made vastly different contributions to capital formation; these contributions in turn were conditioned not only by differences in productivity but also by differences in personal preferences and motivations and social arrangements. I was to encounter similar phenomena in West Africa, in the Levant, in India, and elsewhere.

I should not have been so greatly surprised by what I found. After all, I was aware of the pronounced differences in economic performance among different cultural groups as a feature of much of economic history, and of the fact that groups discriminated against were often especially productive and successful. My temporary oversight was probably due to my having succumbed to the then prevailing view that the less developed world newly discovered by Western economists was somehow different. I had also fallen victim to the notion of the primary and overwhelming importance of physical resources (including capital) as determinants of real incomes—a short period of aberration in which I ignored what I knew of economic history. And I, like others, may have been bemused by figures of average incomes calculated for entire populations without regard to ethnic (and for that matter age) composition.

I might note here that many millions of very poor people in the Third World today, as in the past, have ready access to cultivable land, and also that conventional labor-to-land ratios are meaningless. Such groups as aborigines, pygmies, and various African tribes are extreme cases of poverty amid abundant land. Even in India, much land is officially classified as uncultivated but usable.

The small size and low productivity of many farms in the Third World reflect primarily want of ambition, energy, and skill, not want of land and capital. In any case, it was borne in on me that the notion of uncultivable land is misleading, since cultivability depends heavily upon the economic qualities of the people as well as on official policies affecting the use of land. Examples of the last point include the price policies of governments, control of immigration and inflow of capital, and the terms on which state lands are made available.[5]

Although the discussion of them has been largely taboo in the postwar development literature, the reality and importance of group differences in economic performance cannot be disputed. The subject is virtually proscribed in the profession, even when these differences serve as major planks in official policy, as they do in Malaysia and elsewhere.

5. The distinction between cultivable and uncultivable land is arbitrary. Adam Smith noted that grapes could be grown in Scotland. The arbitrary nature of the distinction is highlighted by the experience of areas such as Holland, Venice, Israel, and other Middle Eastern countries.

Discussion of the reasons for group differences in performance and of their likely persistence would be speculative, and economic reasoning is not informative on these questions. But this provides no excuse for the systematic neglect of group differences by economists. Such differences are plainly relevant for assessment of the economic situation and prospects in Third World countries (and elsewhere too), and for the concept and implications of population pressure. It follows also that the relation between economic development and population growth cannot be examined sensibly on the basis simply of numbers and resources.

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Considerations such as those set out so far have reinforced my reluctance to attempt to formulate a theory of economic development, and also my rejection of theories based either on sequential stages of history or on the conventional type of growth model. The inadequacy of these theories is in any case revealed by their inability to account for the well-attested phenomenon of economic decline (whether absolute or relative). Moreover, economic development is but one facet of the history of a society, and attempts to formulate general theories of history have so far been conspicuously unsuccessful, even though many distinguished minds have addressed the question. Not surprisingly, some of these attempts have yielded informative insights, but none of sufficient generality to serve as a basis for a theory of development.

In the more narrowly economic context, I found the approach embodied in the conventional growth models to be unhelpful and even misleading. The approach focuses on independent variables which I came to know were unimportant. Again, it ignores the interplay between the chosen variables and parameters. Thus, the models take as given such decisive factors as the political situation, people's attitudes, and the state of knowledge.[6] Attempts to increase the stock of capital—for instance, by special taxation or restriction of imports—greatly affect these and other factors treated as parameters, and have repercussions typically far outweighing the effects on development of any increase in capital which might ensue. These shortcomings are apart from basic problems of the concept

6. As I have observed in other places, these growth models have been inspired by Keynes: "We take as given the existing skill and quantity of available labour, the existing quality and quantity of available equipment, the existing technique, the degree of competition, the tastes and habits of the consumer, the disutility of different intensities of labour and of the activities of supervision and organisation, as well as the social structure . . ." (J. M. Keynes, *The General Theory of Employment, Interest and Money* [London: Macmillan, 1936] p. 245). This drastic simplification is doubtfully appropriate even for the analysis of short-term growth in an advanced economy. It is altogether inappropriate to discussion of long-term progress of LDCs.

and measurement of capital, and of the distinction between investment and consumption. This distinction is especially nebulous in the conditions of LDCs, where the use of inducement goods often results in improved economic performance, and consumption is thus complementary to, rather than competitive with, saving and investment.

Since the Second World War an aggregative and quantitative approach has predominated in development economics. Such an approach may have been inspired by the growth models which confine themselves to aggregates such as capital, labor, and consumption. Acceptance of this general approach has had the comforting corollary that the economy of an LDC could be studied on the basis of readily accessible statistics, and also that it was legitimate to dispense with both direct observation and nonquantitative information generally. This neglect in turn has led to an uncritical acceptance of the available statistics. The very large biases in international income statistics, as well as changes in their incidence over time, have been ignored in much of development economics. Again, in the statistics used in development economics, direct capital formation in agriculture has been undervalued or, more often, neglected altogether. Yet this form of capital formation is quantitatively and qualitatively significant in the advance from the largely subsistence activities characteristic of many LDCs. Perhaps more serious in its repercussions has been the failure to recognize this form of capital formation in analyses of economic growth and hence in proposals for promoting growth. Thus fiscal policies for accelerating capital formation have often been advanced without recognition of their necessary effects on direct capital formation in agriculture. In practice, the untoward results of this oversight have been compounded by the habit, itself encouraged by the aggregative approach, of the neglect of prices as determinants of the choice of economic activities.[7]

The use of occupational statistics presents some instructive examples of inappropriate reliance on accessible data and of the neglect, even atrophy, of direct observation. Occupational statistics suggested that in LDCs almost the entire population was engaged in agriculture. For instance, this was a theme of the official reports on West Africa and the literature based on them which I consulted before my first visit. Trade and transport barely figured in the official census or in Lord Hailey's *An African Survey* (London, 1938). I was therefore much surprised by the volume of trading activity and the large number of traders that I was soon able to observe. It became clear that the official statistics were misleading because they did not and could not reflect the prevailing incomplete occupational specialization. In households classified as agricultural it was usual for some of the members to trade regularly or intermittently, regardless of sex and also largely regardless of age.[8]

7. See *Economic Analysis and Economic Policy*, chap. 2; and *The Economics of Under-developed Countries*, chap. 10.
8. See *West African Trade*, chap. 2.

West African experience, which was clearly not unique, except perhaps in the extent of participation in trading, led me to examine and overturn the prevailing Clark-Fisher hypothesis that economic advancement entails a movement of labor progressively from primary to secondary and then to tertiary economic activity.[9] I showed that the theory rested on misleading statistics; that tertiary activities were a miscellany of activities united only by their output being nonmaterial; that they did not have the common feature of high income elasticities of demand, and that many tertiary activities were indeed necessary for emergence from subsistence production in poor countries; that in small-scale trade and transport in LDCs labor can easily be substituted for capital; and that the belief was unfounded that technical progress was necessarily more pronounced in the production of goods than in that of services. Furthermore, the common aggregation of economic activities into three distinctive groups was shown to be of no value for analysis or for sensible policy prescriptions. Yet the notion is still alive that the tripartite classification of economic activities not only is valid and firm but can serve as a basis for policy.

In the general context of development economics, the various preceding examples of misleading aggregation are overshadowed by a practice which I have not yet discussed here. This is the treatment of the world as being two distinct aggregates, the rich and progressing countries and the poor and stagnating countries. The second and much larger aggregate consists of practically the whole of Asia and Africa and the whole of Latin America. This collectivity is envisaged as broadly uniform, caught in a vicious circle of poverty, separated from the rich countries by a wide and widening gap in incomes, and afflicted moreover by generally deteriorating terms of trade in its exchanges with the other aggregate.

In fact, this picture does not bear any resemblance to reality. It does not do justice to the rich variety of humanity and experience in the less developed world, and to the rapid growth of many formerly poor countries and the prosperity of large groups there. The inappropriate lumping together of all so-called LDCs has made it more difficult for economists and others to reject the prevailing notions to which I have drawn attention at the beginning of this chapter, and therefore to recognize the inappropriateness of the policy prescriptions derived from them. I now see far more clearly than I did when my studies began how inappropriate was the division of the world into the two supposedly distinct aggregates.

## [5]

In the early postwar development literature trading activity was very largely ignored. It was ignored in the statistics, in the discussion of de-

9. References to the relevant writings of Colin Clark and A. G. B. Fisher are in *Markets, Market Control and Market Reform*, chaps. 1 and 2, which are revised versions of two articles (with B. S. Yamey) in the *Economic Journal* (December 1951 and March 1954).

velopment prospects, and in the planning literature, as well as in the plans themselves. When considered at all, the discussion of trade was couched typically in perjorative terms. For instance, it was viewed as a hotbed of imperfections and as a source or manifestation of waste. Hence there followed policy proposals for the replacement of private trading arrangements by the establishment of state trading and state-sponsored cooperative societies.

In contrast, the indispensable role of traders, especially in the development of cash crops, was evident in my inquiries both in Southeast Asia and West Africa and in other LDCs I came to know.

I noted what had often been observed by economic historians, administrators, and other observers, that traders provided and extended markets and thereby widened the opportunities open to people as producers and consumers.[10] Traders brought new and cheaper goods to the notice and within the reach of people, a process which induced better economic performance. Sometimes small-scale traders penetrated areas before explorers and administrators had reached them. Without trading activities there could be no agricultural surplus. Traders linked producers and consumers, created new wants and encouraged or even made possible the production necessary for their satisfaction. More generally, they acquainted people with the workings of an exchange economy and the attitudes appropriate to it. By extending people's economic horizons and by establishing new contacts, the activities of traders encouraged people to question existing habits and mores, and promoted the uncoerced erosion of attitudes and customs incompatible with material progress. Moreover, trading widely proved to be a seedbed of entrepreneurial activities extending beyond trading itself. Thus enterprising and successful traders at times initiated or expanded their farming interests (many in any case were part-time farmers). Trading brought to the fore entrepreneurs who perceived economic opportunities and were ready to pursue them. It was not surprising that successful transport and manufacturing enterprises were often established by traders, both local and expatriate.

These dynamic effects of the activities of traders were largely ignored in the postwar development literature. The role of traders in bringing about a more effective interregional and intertemporal allocation of output may have been more widely recognized. But even where this was recognized, the activities of traders and the organization of the trading system were subjected to much misconceived analysis and criticism. For example, the multiplicity of traders and the vertical subdivision of trading activity into many successive stages were often criticized. I showed that these features could be explained by the relative scarcity of capital and administrative skills, the possibilities in trade of substituting labor for capital, and the

10. Since I refer to my observations in the early postwar period, I use the past tense. However, the role of traders still applies generally wherever they are allowed to operate. See *West African Trade*, chap. 2; and *Markets, Market Control and Marketing Reform*, chaps. 1 to 3.

availability of large numbers of people for part-time or full-time trading activity. My observations and analysis of trading activities and arrangements gave rise to much subsequent work by economists and anthropologists. Professor Walter Elkan has gone as far as to suggest that this early work pioneered recognition of the presence and significance of what has come to be termed the informal sector in LDCs, and initiated the study of its economics.[11]

Further, my work enabled me to expose the underlying flaws in familiar proposals and policies for restructuring the trading sector in LDCs. These measures ranged from restriction of the number of traders, and the enforced elimination of particular stages in the chain of distribution, to large-scale state support for cooperative trading and to the suppression of private traders and their replacement by state trading organizations. The adoption of such measures in various LDCs has had the unsurprising consequences of restricting the opportunities for producers and consumers, of entrenching inefficiency in the trading sector,[12] and of obstructing economic progress and the widening of horizons. Most of these so-called reforms have caused widespread hardship and have locked many people into subsistence production.[13]

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Since at least the 1930s both popular and academic literature have decried the fluctuations in the prices of primary products, especially those produced in LDCs. Commodity stabilization schemes have now been major items on the agenda for several decades.

Commodity schemes have usually been proposed as instruments for the reduction of price fluctuations. In practice, however, the objective has usually been the monopolistic raising of prices. This is transparent today when commodity schemes are envisaged as a form of resource transfer from the West to the Third World. But the monopolistic intention was already clear in the interwar regulation schemes, such as International

11. Walter Elkan and others, "The Economics of Shoe-Shining in Nairobi," *African Affairs*, vol. 81, no. 23 (April 1982).

12. It is difficult to explain in retrospect why it was almost universally accepted as axiomatic in the early development economics that cooperative enterprises had such particular economic virtues that they should enjoy extensive state support and protection. A cooperative society is simply a form of economic organization. As such, it does not inherently have access to efficiency superior to that of other types of organization, private or public. If cooperative societies had such attributes, they would not have needed official favors. I discussed these issues fully in *The Economics of Underdeveloped Countries*, chap. 14.

13. See "The Economics of Marketing Reform," in Bauer and Yamey, *Markets, Market Control and Marketing Reform.*

Rubber Regulation. I was to study this in detail and was able to document that, while rubber regulation did not stabilize prices,[14] it did widen fluctuations in output and probably also in producer incomes. Among other untoward effects, it imposed hardship on potential producers who were generally much poorer than were the beneficiaries.

Subsequently, I examined in depth the operations of the official West African marketing boards.[15] These state organizations were given the sole right to buy for export and to export the controlled products. The proclaimed purpose of these arrangements was to stabilize the prices received by producers, and even to improve them. In fact, they promptly developed into a system of paying producers far less than the market value of their produce—they were, in effect, an instrument of heavy, persistent, and discriminatory taxation. Over extended periods they destabilized producer prices and incomes. I drew attention to major effects of this heavy taxation, notably that it reduced the development of cash crops and private savings, obstructed the emergence of a prosperous African peasantry and middle class, and served as a dominant source of money and patronage for those with political power. Thus, paradoxically, although stabilization is typically invoked as cover for the monopolistic raising of producer prices, in this instance it was invoked as cover for persistent underpayment of producers made possible by the monopsony powers of the boards.[16]

My work on rubber regulation and on the marketing boards together had various spin-offs. First, it showed that the smoothing of fluctuations needs to be clearly distinguished from other objectives of official schemes, such as monopolistic raising of prices or taxation of producers by underpaying them. Second, it also showed that even if the reduction of fluctuations was the genuine objective of a scheme, its implementation would run up against formidable conceptual and practical problems. These included the problems of determining on an up-to-date basis the long-term trend of prices; of choosing between the setting of producer prices at the discretion of the authorities or in accordance with an announced formula; of choos-

14. See *The Rubber Industry*, passim, especially pt. 3 and statistical app. 2.

15. See *West African Trade*, pt. 5; and *Markets, Market Control and Marketing Reform*, chaps. 8 and 9.

16. When I first published my findings, they were received with indignation by official spokesmen and by fellow economists. As late as the mid-1950s the supporters of the marketing boards argued that the boards were engaged only in price stabilization. By the 1960s it was widely accepted that they were, and had been all along, instruments of taxation. It is also now generally agreed that the proceeds of this taxation were in large measure wasted.

The marketing boards were to a considerable extent descended from largely unsuccessful private produce-buying cartels; state monopsonies were introduced at the instigation of members of these cartels. See my *Dissent on Development*, essay 12; the original version appeared in *Journal of the Royal Statistical Society* (1954), pt. 1.

ing between stabilization of prices and stabilization of producer incomes; and of choosing the frequency and amplitude of the adjustments in producer prices. Third, my work and the response it elicited from Professor Milton Friedman[17] led me to question whether the exercise of government power was desirable or necessary for producers to achieve price or income stabilization if they felt the need for it. If stabilization of disposable incomes is desired, producers on their own account can set aside reserves on which to draw in times of adversity. If necessary, they can form voluntary associations to help them achieve this purpose.

## [7]

The truth of the French saying, "rien ne vit que par le détail," impressed itself upon me in the course of my work in Southeast Asia and West Africa. Much of this work uncovered phenomena and relationships which had not been acknowledged adequately either in previous studies of these regions or in the more general economic texts. I list briefly a number of these matters not already discussed in this essay; fuller treatments are to be found elsewhere in my publications. However, several of the issues raised or illustrated are of some general significance and interest.

The supply of smallholders' rubber had commonly been instanced as a classic case of a backward-sloping supply function. In fact, it was possible to establish not only that the supply curve was forward-rising but also that this was fully recognized in the implementation of official policy (for instance, in the imposition of special export taxes to curtail smallholders' exports under rubber regulation). The much higher density of planting on rubber smallholdings than on the estates used to be attributed to the crude methods used by smallholders. In fact, it could be shown to reflect differences in the availability of factors of production to the two broad groups of producers. Further, even the short-period supply price of rubber could not be estimated simply by reference to current outlays, but had also to include the expected reduction of future revenues through the current consumption of the latex-containing bark. Again, cost of production was found to vary greatly with the current product price (much more so than with the scale of operations). Thus cost of production, and therefore the supply price, depended significantly on expected future prices as well as on current prices.[18] When it is recognized that current and prospective product prices affect costs, it is then not legitimate to treat supply as independent of demand (as is the standard practice in microeconomic theory).

I found that the standard expositions of monopoly and of its measure-

17. Milton Friedman, "The Reduction of Fluctuations in the Incomes of Primary Producers: A Critical Comment," *Economic Journal* (December 1954).

18. On the supply of rubber, see *The Rubber Industry*, chap. 4 and app. E.

ment were incomplete, even misleading. Rubber regulation covered many thousands of producers, none of whom controlled even 2 percent of total supplies of a highly standardized product or had any influence on prices. The controlling authority, on the other hand, faced a much less than perfectly elastic demand. This combination was very different from the situation typically analyzed in monopoly theory. In the study of West African trade, statistics accessible to me showed that the degree of concentration was systematically higher for standardized products than for differentiated products. This was contrary to what I expected to find from contemporary discussions of product differentiation. In both Southeast Asia and West Africa the number of trading points diminished steadily from the urban centers to the outlying rural areas. Yet I found this to have no systematic relation to the intensity of competition: the effective degree of monopoly could not be predicted at all reliably from the number of traders present. The small trader in a remote village was exposed to competition from many sources, including itinerant peddlers and farmers acting as part-time traders. The number of traders, however, became important in determining the strength of competition whenever entry was officially restricted. Even then, diversity among the traders (such as ethnic diversity or differences in length of establishment) could modify the effect of numbers on competition.

That detailed statistics can be revealing was shown by statistics of the prices of official rights to export rubber from Malaya. These could be made to reveal both the de facto extent of restriction and the very low supply price of large quantities of smallholders' rubber. Closer examination of the statistics of total estate production and those of locally registered companies disclosed that rubber regulations treated U.K.-registered companies more favorably than locally registered companies, and estates more favorably than smallholdings. The statistics could be used also to measure the effect of the 100 percent excess profits tax on the level of production.

Direct observation in conjunction with certain statistical series, especially transport statistics, helped to uncover the large volume and importance of kola nut production and trade in Nigeria, activities entirely in the hands of Africans and virtually unremarked in official and other publications. Again, detailed examination of the working of import and price controls in wartime and postwar West Africa made clear that quite momentous political and social consequences could follow from apparently innocuous official measures.

## [8]

During the latter part of the 1950s I first wrote on two major issues in development economics: comprehensive planning and foreign aid. I was subsequently to develop my analysis and conclusions when these two subjects came to loom more largely both in the academic development literature and even more in public discussion. I noted then that comprehensive central planning was certainly not necessary for economic advance; it was much more likely to retard it. It did not augment resources, but only diverted them from other public and private uses. It reinforced the authoritarian tradition prevailing in many LDCs. And it also divorced output from consumer demand and restricted people's range of choice.

On foreign aid I wrote little, beyond saying that it was not indispensable for the progress of poor countries and that it often served to underwrite and prolong extremely damaging policies commonly pursued in the name of comprehensive planning.[19]

I see no reason to retract the findings and assessments set out in this summarized version of my earlier writings. But I must acknowledge a serious misjudgment. I failed then to appreciate the pervasive significance of the politicization of economic life in LDCs. Except in my treatment of the West African marketing boards, I was apt to analyze the more specifically economic implications and effects of individual policy measures without appreciating adequately how they contributed to the general politicization of life in many LDCs. By the late 1950s the principal measures included state monopoly of major branches of industry and trade, including agricultural exports; official restrictive licensing of industrial and other activities; controls over imports, exports, and foreign exchange; and the establishment of many state-owned and state-operated enterprises including state-supported and state-operated so-called cooperatives. Several of these individual measures gave governments close control over the livelihood of their subjects. When applied simultaneously, these measures conferred even greater power on the rulers.

In these conditions the acquisition and exercise of political power became all important. The stakes, both gains and losses, in the struggle for political power increased. These developments enhanced uncertainty, anxiety, and political tension, especially in the many LDCs which comprised distinct ethnic, religious, or linguistic groups. They thereby diverted people's energies and resources from economic activity to the political arena.

These developments and their repercussions have become much more pronounced and widespread since the 1950s. Not only the economic but even the physical survival of large numbers of people have come to depend

19. My subsequent writings on planning and foreign aid can be found in *Dissent on Development* and in *Equality, the Third World, and Economic Delusion* (London: Weidenfeld and Nicolson; and Cambridge, Mass.: Harvard University Press, 1981). I have returned to these two subjects in my book, *Reality and Rhetoric: Studies in the Economics of Development* (London: Weidenfeld and Nicolson; and Cambridge, Mass.: Harvard University Press, 1984).

on political and administrative decisions. Productive ethnic minorities have been conspicuous among the victims. What I saw only dimly in the 1950s has therefore become a major theme in some of my more recent writings.

# Comment

## Michael Lipton

In 1946 a young economist, hired by the British Colonial Office, visited Malayan rubber smallholdings. His *Report* truly lived in its details. Unlike many others before and since, he did not overrepresent roadside farms and thus avoided biasing his enquiries; he did cross-check reports of income and outlay within each interview; and, above all, he acquired a deep technical understanding of the crop under study. This allowed him to explain why rules that prohibited new rubber planting, but allowed replanting, unfairly and inefficiently helped big estates at the expense of smallholders.[1] He shows how rubber smallholdings contained both highly efficient growth potential and the best chance of self-improvement for the working poor, yet were held back to protect powerful and relatively inefficient European-owned estates.[2] The tools of bias included policy and research skewed against smallholders; local trading monopoly; and government failure to engage in competing trade, to provide inputs and research for smallholder needs, to ensure the representation of smallholders on crucial decisionmaking bodies, and even to protect smallholder land against waterlogging.[3] To remedy these deficiencies the author proposes, among other things, specific, promising, and imaginative government involvements.[4] Is this, too, Peter Bauer?

In his work (as in Bartok's ) one has to reconcile three periods: the involved, creative fieldwork of youth; the increasingly confident, general

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1. P. T. Bauer, *Report on a Visit to the Rubber-Growing Smallholdings of Malaya, July-September 1946* (London: Colonial Office, 1948), pp. 10, 11, 25.
2. Ibid., pp. 23, 64, 44. Bauer's passionate and specific concern for the fate and prospects of the poor in this document (see especially p. 27, para. 144) contrasts strikingly with some of his more recent general writing about, for example, "relief of poverty or some other purpose unrelated to development" (P. T. Bauer, "Foreign Aid and Its Hydra-headed Rationalizations," in *Equality, the Third World, and Economic Delusion* [London: Weidenfeld and Nicolson, 1981], p. 101).
3. *Report on a Visit to the Rubber-Growing Smallholdings of Malaya*, pp. 40–57, 60–63.
4. Ibid. and pp. 64–65, 87–90.

and provocative, but also strident and (as it were) supra-empirical middle period; and, in maturity, mellowness. In the present paper, aid and planning are once more neither indispensable nor sufficient for development—not, as in the middle period, its implacable enemies.[5] However, this new paper contains enough "middle Bauer" for us to contrast it, usefully, with the earlier practical experience and theory building.

Lord Bauer is a *classical* economist. Enterprise, trade, enlargement of markets: these are the engines of development. Bauer makes no neoclassical claim that all businessmen act like profit-maximizers, or would maximize welfare if they did. For Bauer, it is the move from subsistence to ever larger markets that counts. His early Malayan work combined this classical emphasis on the role of trade with awareness of "sporadic buyers' rings," of "unduly high dealers' margins," and hence of the need for a larger number of competing "Government buying stations."[6] Perhaps because of his growing fear of politicization, Bauer has recently muted this classical stress on the need for the state to protect the poor from trusts—on Adam Smith's perception that "People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices."[7] Bauer's work shows, nowadays, little Ricardian fear that rising shares in GNP of differential rent or monopoly quasi-rent—whether to OPEC, landlords, or formal industry—may erode rewards to, or finance for, enterprise.

Nevertheless, Bauer's generally classical approach is exemplified by his opposition to barriers against trade, investment, and migration and by his tributes to "individual voluntary responses of millions of people to . . . opportunities created largely by external contacts and brought to their notice . . . primarily through the operation of the market." This theory of development is backed by Bauer's Malayan and West African evidence of extremely widespread entrepreneurial, especially small-farmer, response; Bauer was one of the first to show, and to insist against the researchers in the capital cities, that small farmers are shrewd profit-seekers and effective innovators, often outperforming large estates. Before Hirschman, he stressed that such people's investments might precede, not follow, infrastructure.[8] (One might add that the wrong sort of infrastructure—for instance, a premature access road, effectively subsidizing mass-produced competition—frequently nips such local enterprise in the bud.)

However, there is an odd thing about Baverian classicism. It is the

5. P. T. Bauer, *Dissent on Development* (London: Weidenfeld and Nicolson, 1971), pp. 69–94.

6. *Report on a Visit to the Rubber-Growing Smallholdings of Malaya*, p. 61.

7. Adam Smith, *The Wealth of Nations*, 1st ed. 1776 (New York: Modern Library, 1937), p. 128.

8. See A. O. Hirschman, *Strategy of Economic Development* (New Haven, Conn.: Yale University Press, 1958).

attempt *both* to believe in this market theory of development, *and* to reject "general theories of history" in common with the Hayek–Popper–London School of Economics school. The gap between classical theory and anti-theory is to be bridged in two ways. Neither is satisfactory.

First, Bauer—while advancing a particular, data-based account of quasi-classical development in specific countries—rejects both general, formal macro models of development and their data base.[9] That rejection depends on his views that the variables in these models are relatively unimportant, a matter to which I revert later; and that the data are no good. The latter objection, for most of Asia and Latin America, is out-of-date. We now know a good deal about important quantities that used to be left unmeasured. Self-consumed farm output has been included (by means of crop-cutting samples) since the early 1950s. Rural nonfarm employment, long measured in India, has now been assessed in many micro environments elsewhere—even for people who are mainly farmers.[10] "Biases in international income statistics," a recurrent concern of Bauer's, have been corrected by moves toward a purchasing-power comparison at least since the late 1950s; such corrected data (due to Kravis's work under World Bank auspices) are now available for many developing countries.[11] In any case, if the data were no good, we should have no reason to accept or reject any of Bauer's three approaches: his early account of quasi-classical growth (albeit with some state intervention) in specific cases; his later claims that such growth, without aid or planning, was in most cases the best chance for development; or his denial that *any* development path can be generally valid. Models and data, explicit or implicit, are the only way to test theories against each other.

Second, Bauer rejects metatheories, which might imply endogenous, socioeconomic explanations of why quasi-classical development paths sometimes work and sometimes fail. He does so because the *chance* that particular countries happen to be inhabited with particular cultural or ethnic groups is to him crucial. He argues, for instance, that Chinese rubber tappers work harder than Indian ones, and that some groups just

9. See both the present paper and *Equality, the Third World, and Economic Delusion*, pp. 262–66.

10. Enyinna Chuta and Carl E. Liedholm, *Rural Non-Farm Employment: The State of the Art*, MSU Rural Development Paper no. 4 (East Lansing: Michigan State University, Department of Agricultural Economics, 1979); and recent rounds of the Indian *National Sample Survey*.

11. This process started in the 1950s with the Milton Gilbert and Irving B. Kravis studies for the Organisation for European Economic Co-operation (now the OECD). The World Bank's International Comparison Project, under Dr. Kravis's guidance, already covers about twenty-five developing countries. The latest publication, containing references to the earlier work, is Irving B. Kravis, Alan Heston, and Robert Summers, *World Product and Income: International Comparisons of Real Gross Product* (Baltimore, Md.: Johns Hopkins University Press, 1982).

are "especially productive and successful."[12] Although such claims—they are hardly explanations—should indeed be researched and not "proscribed,"[13] careful enquiry almost always reveals endogenous and temporary, not exogenous and hereditary, determinants of "group differences in economic performance" (for example, in the Punjab[14]). Moreover (especially in a world of intermarriage, migration, Galtonian "regression toward the mean" of genetic characteristics, and integrated gene pools), such explanations as "Group X works harder" are very unsatisfactory. They are residual—confessions of ignorance. People believed God caused lightning directly, until the explanation was discovered scientifically.

Bauer is forced to oscillate between classical theory and anti-theory for a most interesting reason. His early work was on some developing, export-crop-based economies of Southeast Asia and West Africa. There, the presumptions for the classical model were largely fulfilled. The export crops attracted "investment by European enterprises" in estate development in Southeast Asia and "extensive capital [from] European trading firms" in West Africa. Attractive prices for those crops, "largely empty" cultivable land, and (initially at least) high income- and price-elasticities of demand then permitted widespread entrepreneurial response by indigenous smallholders. In Malaya, Bauer courageously sought to get the colonial state, largely representative as it was of European big capital, off the smallholders' backs, so they would not be prevented from planting more rubber or from obtaining relevant research and inputs.[15] In West Africa, as Bauer showed[16] (but increasingly since his warnings), expansion prospects have been set back by marketing boards and other devices, purportedly for stabilization, but in reality to transfer resources from dynamic, poor farmers to the burgeoning, inefficient apparatus of the urban state.[17] *Few, if any, parts of today's developing world, however, are*

12. Some particularly regrettable reflections on the alleged incapacity of certain U.S. American Indians to develop appear, without evidence, in *Dissent on Development*, p. 97.

13. It is no more—and no less—disgraceful to shout down the arguments for inherited (and even perhaps racially specific) indicators of intellectual capacity, than it is to accept these propositions without testing them properly, or to assume that *even if true* (and the evidence appears to show that they are false) they could justify discrimination against a group of human beings on the grounds of low IQ, hereditary or environmental, average or median or top-percentile.

14. M. S. Randhawa, *Green Revolution* (New York: Wiley, 1974).

15. *Report on a Visit to the Rubber-Growing Smallholdings of Malaya*, passim, especially pp. 87–90.

16. P. T. Bauer, *West African Trade* (London: Routledge and Kegan Paul, 1963); "Operations and Consequences of Statutory Export Monopolies of West Africa," *Journal of the Royal Statistical Society*, vol. 1 (1954).

17. Michael Lipton, *Why Poor People Stay Poor* (Cambridge, Mass.: Harvard University Press, 1977), pp. 294–96.

*like the export-crop economies of, say, Malaya or the Gold Coast in the late 1940s in the relevant respects.*

Hence Lord Bauer is, in my view, constantly compelled to throw rather flimsy intellectual bridges from his early work—in countries where resource endowments and market opportunities attracted private foreign capital to initiate indigenous growth, in a way reminiscent of the classical thesis—to other developing countries. Bauer recognizes that, despite many different policies, few such countries have spread development to vast numbers of exporting smallholders, as did Malaya and Ghana.[18] Hence classical paths cannot be a *general* predictive base for development theory. Remembering Malaya and West Africa in the 1940s, Bauer both insists on the validity of the classical pattern, and develops reasons—ethnic, cultural, or metatheoretic—why *no* pattern can be expected to apply everywhere.

The problems that result are nicely, and jointly, pinpointed by Bauer's treatment of overseas capital, aid, commodity agreements, Harrod-Domar models, and vicious circles of poverty. Export-crop production and trade in Dutch and British colonies in some areas received significant inflows of private foreign capital from 1900 to 1940. The local farmers and traders in a few such areas—having much spare land and enjoying population growth well below present rates in poor countries—built significant growth, quite widely shared, upon these inflows. Because rubber (and tin) and, in the early stages, cocoa and robusta coffee faced promising markets, international commodity cartels—or even agreements—were nuisances, not necessities. But were these realities too specific and temporary to allow us to transfer the lessons to other situations? If so, does Bauer's attachment to the classical market model force him to reject generalization, aggregation, even theory itself, in order to reconcile the early successes he knew in detail with the biased, unsatisfactory, partly planned, partly aided, but undoubtedly growing and developing realities of the past three decades?

We can usefully start with Bauer's remark that "conventional growth models" focus on "variables which I came to know were unimportant." These explanatory variables are, typically, domestic and foreign savings and investment. These are linked in conventional models to growth via the propensity to save and the marginal productivity of capital. (All this can be, and often is, disaggregated ad lib.) In Bauer's youthful studies, private foreign capital—for planting or trading—came in to develop and exploit major new export-crop opportunities on empty land. The variables of the conventional growth models—savings, investment, productivity of capital—indeed seemed "unimportant" because their values were overwhelmingly favorable.

18. Polly Hill, *Migrant Cocoa Farmers of Southern Ghana* (New York: Cambridge University Press, 1963).

"Rapid economic progress" involving "large-scale capital formation in agriculture by the local people," says Bauer, "cannot be squared with the idea of the vicious circle of poverty and stagnation." On the contrary: shared progress if there are initial capital inflows and subsequent widely spread opportunities, and vicious circles of stagnation if there are not, are two different ways of stating the same point. The Indian Punjab, despite the massive early investments of the government in irrigation and extension and research, since 1960 tells a similar story of progress. With favorable natural resources (especially favorable ratios of good land and improved techniques to people), initial nonlocal capital inflows, and promising markets, both the marginal productivity of capital and the propensity to save will be high enough to attract major domestic savings, embodied in productive investments.

These variables, when very favorable, seem "unimportant"—but they interact to help LDCs break out of the vicious circles. When circles remain vicious, the "unimportant" variables are unfavorable: in Madhya Pradesh or the Sahel or Bangladesh, private domestic savings ratios *are* kept down by low incomes, which *are* perpetuated by underinvestment because of low savings, so that planned public or aid-based funds become vital to supplement the savings and to raise the productivity of capital through research and training. (Incidentally, both savings and investment can easily be redefined to include outlays on health and education.) In these places, again in a vicious circle, hunger depresses productivity, which in turn keeps down food production and maintains hunger. *Opportunity*, as in Bauer's experiences of West Africa and Southeast Asia, is needed to attract the initial inflow of private capital, and the local response to it, in order to reverse the vicious circle of stagnation—to turn it into a virtuous circle of higher savings rates, more investment, higher incomes, then more savings again; or higher labor productivity, more food, less hunger, and higher productivity again.

Consider the opposite extreme to the lands of Bauer's youth, to those ideal places and times to serve as test cases for classical development. Consider Bangladesh today. Big private capital inflows are very unlikely. This is because Bangladesh's main export crops, jute and tea, face highly price-inelastic and income-inelastic market demand.[19] Instability superimposed on such gloom is unattractive to investors, at least until there is a reliable international commodity agreement. Moreover, Bangladesh's ratio of people to good land is so high (and so dynamic) that spare land for

19. Although demand for Bangladesh's two main exports, jute and tea, is highly price-inelastic (in each case about minus 0.33), Bangladesh looms so large in the world jute supply that its *own* revenue falls if it increases output and exports of jute. In the case of tea, Bangladesh's share in world exports is very small, but revenue gained from extra production is offset by a loss, about twice as large (because price-elasticity of demand is minus 0.33), in revenue for other tea exporters, all developing countries.

*any* crop is almost nil.[20] In addition, the people in Bangladesh (unlike those in Malaya and Ghana in 1945) are almost all too poor to save much. With population growth approaching 3 percent, average income barely above the poverty line and hence little domestic savings capacity, and marginal capital-output ratios of at least 3, circles do hiss viciously whatever one's suspicions of such aggregates, especially since many people are so hungry that their productivity as food growers suffers. All the components of the classical growth pattern—initial foreign capital inflows, promising and elastic export-crop markets, spare land, and people able to finance savings to transform it—happily typified the countries that formed Lord Bauer's mental set. All are missing in Bangladesh: circles *are* vicious; capital and saving, and the parameters linking them to output and income respectively, *are* crucially important; large concessional inflows of capital *are* necessary (though not sufficient) to turn the vicious circles into virtuous ones; and inelastic commodity demands, by imposing unfavorable price trends upon unpredictable instability, *do* render the control of such instability through international commodity agreements important and desirable, though probably not essential to development.

Lord Bauer has contributed great insights into the real possibilities, in lucky places, of classical development paths. Other lucky places such as the Republic of Korea and Taiwan, because forced by the occupying power to redistribute land rights to efficient small farmers (and because supplied by that power with massive aid and fairly open access to markets), have subsequently made a success of something like a neoclassical path, albeit modified by initially heavy trade protection, persistently pervasive planning of credit and investment, and some political repression. At the other end of the spectrum, a Cuba or a China can also credibly claim to have abolished most of its absolute poverty—but in ways that combine inefficiency, often negative growth, and, once again, political repression. Much the most interesting cases, in my view, are places such as Sri Lanka, Costa Rica, and some states of India, where public sector action has successfully and substantially reduced poverty, yet where—despite great, persisting inefficiencies and inequities—both real growth and political freedom persist. All get some foreign aid and some private capital. None fits neatly into anyone's model of development. But the search for general theories must go on.

20. In most of Indonesia, Egypt, India, and Bangladesh, the statement that "small size and low productivity of many farms in the Third World reflect primarily want of ambition, energy, and skill, not want of land and capital" is wholly inapplicable—not least because, as with Bauer's Malayan smallholders, smaller farms almost always produce more net value added per acre than large ones (R. A. Berry and W. R. Cline, *Agrarian Structure and Productivity in Developing Countries* [Baltimore, Md.: Johns Hopkins University Press, 1979]).

# Comment

T. N. Srinivasan

LORD BAUER HAS ONCE AGAIN succeeded in being provocative in this remembrance as in most of his earlier writings. While he has not changed his views of the development process over a period of three decades, except for admitting a single serious misjudgment in not appreciating the pervasive significance of the politicization of economic life in the less developed countries, he has presented an expurgated version of them here. For an unvarnished, no punches pulled version, one has to read a collection of some of his writings published in 1981.[1]

It is difficult to quarrel with his summary of the early development literature. However, it is worth recalling that many of the pioneers, particularly those from the relatively advanced developing countries, viewed the problem as one of achieving in one or two generations a level of development that it took several generations to achieve in the developed countries. Further, the only experience of such rapid transformation that was then available was that of Soviet planning. With hindsight, of course, one may fault some of the early writers for their naiveté in believing that a Soviet-style central economic planning is possible in a less developed country without a Soviet-style political structure.

Bauer has conveniently summarized his own views of the process of development in section 2 of his paper. However, his review of Ali Mazrui's book, *The African Condition*, is far more revealing. While many thinkers in the developing world viewed economic and social development as a process of modernization in the sense of applying scientific methods and technology without giving up traditional values, Bauer views it differently: "The concept of material progress, of steadily increasing control of man over his environment, is Western, as are the modes of conduct which derive from it. . . . But the ideal of modernization without Westernization is self-contradictory."[2]

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1. Peter Bauer, *Equality, the Third World, and Economic Delusion* (London: Weidenfeld and Nicolson, 1981).
2. Ibid., p. 205.

Pioneers such as Theodore Schultz have emphasized that human capital formation—the development of education and skills as well as of institutions that provide incentives and allow individuals to respond to them—are crucial in modernization. Bauer states:

> African backwardness amidst ample natural resources is only one conspicuous example of the fact that material progress depends on personal qualities, social institutions and mores, and political arrangements which make for endeavour and achievement and not simply physical resources. The relative lack of able and effective people is crucial.[3]

But for Bauer the economic argument is not enough. He proceeds to link inadequate human capital formation to what one may euphemistically call "national characteristics and attitudes." For instance, he cannot resist pointing out that

> In historical times the achievement of Black Africa [that is, most of the continent of Africa] has been negligible compared with that of Asia and Europe. This in no way justifies enslavement or humiliation. . . . Before the closing decades of the nineteenth century [Africa] was without the rudiments of civilized or modern life. For instance, before the arrival of Europeans in sub-Saharan Africa all transport was by muscle, almost entirely human muscle unaided by the wheel. . . What Shiva Naipaul says about Zambia in his recent book, *North of South: An African Journey*, applies widely in Black Africa: "Expatriates staff the mines, the medical services, the factories, the technical colleges, the universities. Without them, the country would fall apart. Zambia makes nothing; Zambia creates nothing. The expatriate lecturer in English waved apologetically at the handful of books, perhaps half a dozen on the library shelf. 'There,' he said, 'that's it. That's all the Zambian literature there is.' For him, the paucity is a source of genuine embarrassment. 'I would dearly love to teach something Zambian to my students. But what can I do if there's nothing.' "[4]

This penchant for tarring a whole continent of nations with a single brush leads Bauer to assert

> Some of the attitudes in India which are most adverse to material change are indeed unique to the country are especially pronounced there, such as the operation of caste system, the veneration of the cow, the reluctance to take animal life, and contemplative, non-experimental outlook.
>
> Although Indians have many valuable economic qualities, especially when they are not hampered by a very restrictive social environment, they are nevertheless generally less ingenious, energetic, resourceful and

3. Ibid., pp. 193–94.
4. Ibid., pp. 194–95.

industrious than the Chinese, as is suggested by the relative performance above of Chinese and Indian emigrants.[5]

It is an elementary fact that in an appropriate environment, the non-development-oriented attitudes somehow tend to disappear, if they were indeed constraints. After all, until recently in the span of history, many Western observers held Bauer-like views of the Japanese! Jagdish Bhagwati quotes the following from a report written in 1915 of an Australian expert invited by the Japanese government:

> My impression as to your cheap labour was soon disillusioned when I saw your people at work. No doubt they are lowly paid, but the return is equally so; to see your men at work made me feel that you are a very satisfied *easy-going race* who reckon time is no object. When I spoke to some managers they informed me that it was impossible to change the *habits of national heritage*.[6] [Emphasis added.]

Bauer's policy recommendations are predictable: a severely limited role for government, almost exclusive reliance on the market, including reliance on world capital markets rather than foreign aid for external capital needs, and so on. Although he believes that the West can contribute to the Third World development by reducing its barriers against Third World exports, he is more cautious on the free movement of people. If trade liberalization makes substantial headway, he is willing to consider "conditions under which freer immigration policy might be practical in certain countries."[7]

He believes that foreign aid should be left to voluntary charitable agencies. It should be in the form of cash grants for projects. His views on funding for the International Development Association and on World Bank research are worth quoting:

> In June 1976, a referendum was held on a Swiss government proposal to provide substantial funds to the official International Development Association for handouts to Third World governments. The proposal was heavily defeated and at the same time, the Swiss voluntarily contributed large sums to a fund for the victims of an earthquake in Italy as well as to many Third World charities. Thus the public can distinguish official aid from voluntary charity. . . .
>
> Over the imprint of the Bank, senior staff members have been able to publish reports and studies which are riddled with simple violation of common sense, fact and logic. The paucity of critical comment, indeed

5. Peter Bauer, *United States Aid and Indian Economic Development* (Washington, D.C.: American Enterprise Institute, 1959), pp. 23, 112.

6. Jagdish Bhagwati, "Development Economics: What Have We Learnt?" Distinguished Speakers Lecture, Manila, Asian Development Bank, October 1983.

7. Bauer, *Equality, the Third World, and Economic Delusion*, p. 131.

> often the commendation of altogether incompetent World Bank publications, reflects in part the prestige and strength of the Bank, and in part the approval of its ideology by the academics and the media. The Bank has given aid used to support inhuman and coercive policies in the Third World—all without endangering the position or prestige of the Bank and mostly without eliciting critical comment.[8]

While I agree with Lord Bauer that a much greater reliance on markets is called for in many developing countries, I find in his writings more polemics and debating points than depth. A far deeper analysis of the role of markets and development can be found in the few pages of Kenneth Arrow's presidential address to the American Economic Association. A fascinating historical analysis of why Europe developed while India and China did not is available in a book by an Australian economic historian, E. L. Jones.[9] I confine myself to Professor Arrow's discussion.

He pointed out that while "the now demonstrated fact that flexible exchange rates are a feasible way of conducting international finance is a triumph of theoretical insights over practical men's convictions," one of the two major failures of neoclassical economics as an explanatory mechanism has been "the incompatibility of recurrent periods of unemployment in the history of capitalism with a neoclassical model of general market equilibrium." The other failure identified by Professor Arrow is of greater interest for my present purposes. He argued that

> inequality in economic development among countries, and among groups and regions within a country, provides a second and somewhat complicated difficulty for neoclassical theory. A purely neoclassical answer would explain differences in per capita income by differences in physical and human assets per capita. This, of course, raises the further question, how this came to be, which would require a fully dynamic model to answer. But the more compelling problem is that the differences in income seem too vast to be explained by factor differences. Indeed, in the presence of international trade, and especially international capital movements, wage differences should be strongly reduced compared to what would occur in autarkic states . . .[10]

Professor Arrow suggested that differences in the production-possibility sets of different countries could be a possible answer, only to dismiss this as a partial answer in that it raised further questions, for the differences in production-possibility sets among contemporaries can be due only to constraints on the transmission of knowledge, in a broad sense, across national boundaries. This led him to put his finger on the failure of

8. Ibid., pp. 129, 131.
9. *The European Miracle* (New York: Cambridge University Press, 1981).
10. Kenneth J. Arrow, "Limited Knowledge and Economic Analysis," *American Economic Review* (March 1974), pp. 1–10.

markets for future goods, in part because of large enforcement costs with respect to future contracts as compared with contemporaneous contracts, and in part because of the many uncertainties about the future. In particular, the markets of credit and capital goods, he suggested, are most likely to be subject to imperfections or even nonexistence. And nonexistence or imperfection of even a single market has spillover effects on other markets and can destroy the optimality of competitive equilibrium.

Once nonexistence or imperfect functioning of markets is admitted, the normative characterization of a global competitive equilibrium as reflecting an efficient and Pareto optimal allocation of resources among countries and individuals no longer holds. If markets fail, Professor Arrow argued, other social devices are likely to be invented, such as government intervention, codes of conduct for economic agents, or economic organizations with some power between the neoclassical competitive firm and an all-encompassing government.

One of the more exciting areas of current research involves investigations into the role of alternative institutional and contractual arrangements that exist in the absence of a complete set of insurance and future markets. In fact, the various types of land tenancy, labor hiring, credit, and selling arrangements observed in developing countries are institutional responses to the absence of markets. A fuller understanding of their systemic role in concrete sociopolitical-economic contexts is essential in devising developmental policies. In the absence of such understanding, a discussion of the place of markets or, for that matter, central planning cannot go very much beyond assigning totemic value to either. Further, since governments, just as markets, can be and often are imperfect, and are subject to lobbying, interventions to correct market imperfections that are optimal in theory may turn out to be worse than no interventions at all. Rather than fulminations against government intervention, such as Bauer has given us, we sorely need an analysis of development which treats the government as *one* of the many forces that influence its course and which draws on the rich comparative country experience and data that the World Bank must surely have.