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PROFESSOR BAUER ON DEVELOPMENT*

A review article

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Bauer's views on vicious circles, the 'widening' gap between rich and poor countries, central planning, foreign aid and the appeal of Marxism in less developed countries are summarised. There is a discussion and summary of an appropriate analysis of the issues raised by Bauer. Attention is concentrated on the evidence related to a 'widening' gap, the potential failures of the price mechanism and the effects of foreign aid. It is suggested that Bauer's analysis is superficial, even though this may also be true of some he criticises, and that the case for aid remains strong.

1. Introduction

Professor Bauer's views are widely seen by aid lobbyists as damaging to their position. The analysis and work on which these views are based are probably less well known. We have recently had the opportunity to gain a broad perspective on Bauer's writings since he has collected over twenty of his essays, written during the nineteen-sixties, into one volume *Dissent on development.*[1] The purposes of this paper are to give a summary and appraisal of Bauer's main arguments and then to review the case for aid.

We begin with a summary of Bauer's views. As the title implies, the book consists largely of an assault on, what he sees to be, the prevailing orthodoxy. He also speculates on the origin of various economic doctrines as he tries to understand the motives of those who put the arguments he finds so objectionable.

The second part of this paper is devoted to an appraisal of Bauer's arguments. This does not mean that we attempt to decide, for each issue, whether Bauer or those he criticises is right. The reasons are as follows. Many of the arguments that are commonly advanced for the positions Bauer attacks are weak. The problem is that Bauer's attacks are often inconclusive because their target is

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[1] Bauer (1971).

some of these arguments and not the policies themselves. The appraisal, therefore, takes the following form. We first give our own view of how an analysis of the relevant issue or policy should proceed and, where possible, outline the conclusions from such an analysis. We can then evaluate Bauer's discussion and (occasionally) the case that has hitherto been offered for the position he opposes.

The discussion of the case for aid follows similar lines, but is separated into a third section since it may be the main concern of some readers and rests on some of the conclusions of the previous appraisal.

At times the analysis is conducted at a level more detailed than that of Bauer for he concerns himself with grand issues – notably planning versus the free market – and deals in generalisations. But theoretical generalisations need specific hypotheses and careful argument, and empirical generalisations an appropriate discussion of the relevant data. Bauer subjects few of his statements to these tests.

2. Summary of Bauer's book

The first part of the book is on ideology and experience and deals with the notions of the vicious circle of poverty and the widening gap between rich and poor countries, the cases for central planning and foreign aid, and the appeal of Marxism in less developed countries.

Bauer argues that the existence of vicious circles is refuted by examples of countries that have advanced rapidly and some that are advancing rapidly (for example, on p. 34, he quotes the statistic that the GNP per head of Latin American countries as a whole grew by 2.4% p.a. over 1945–55 – faster than for the U.S.A. over the same period). On the 'gap' he argues that spurious statistics have been used, that there has been little analysis of the *ratio* of per capita incomes in rich and poor countries and that over-aggregation has allowed the slow progress of countries such as India and Indonesia to mask the rapid advance of such countries as Japan, Thailand, Kenya and those in Latin America. He suggests that the vicious circle and the gap are ruses for promoting aid.

He attacks those who would argue that comprehensive planning is indispensable for progress with examples of countries that have progressed with little planning. According to Bauer, planning results in concentration of power, the stifling of initiative and the diversion of potentially creative energy into unproductive politics. The demands of consumers are ignored and resources misallocated. The claim that planning is essential for development is motivated by political bias and the search for power.

Foreign aid, he suggests, is neither necessary nor sufficient for development. Some countries' economies have grown rapidly without aid, whereas others have progressed slowly while receiving much aid. Aid promotes a sense of dependence on others which damages initiative. It leads to attitudes, policies and institutions, often transferred from donor to recipient countries, which are harmful to develop-

ment; for example, foreign-style universities and a lack of concern with balance of payments difficulties. Since aid is a free gift from outside, it is more likely to be squandered by the recipient than funds borrowed from outside or raised by domestic saving. He suggests that if the ability to use aid beneficially were really present then loans could be raised and repaid without difficulty.

UNCTAD and Raul Prebisch come under fire for their argument that the export earnings of poor countries have an inherently low growth potential and thus aid is necessary for foreign exchange. Bauer claims that balance of payments problems are usually of a country's own making and that export possibilities are often much better than is pretended.

He also devotes some space to the moral and political arguments. Aid, he says, is an admission of responsibility for the backwardness of the recipient countries when no such responsibility exists. In support, he argues that the most backward countries are those with the least external contacts. There can be no moral uplift to be gained from aid since it is a compulsory transfer of the taxpayers' money. It is often regressive in the sense that the resources of the poor in rich countries go to the rich in poor countries. He claims that the poverty of potential recipient countries should not be a criterion for aid since such arguments can lead to peculiar conclusions. For example, if poverty is the criterion one would advocate an increase in aid to governments that expel groups whose productivity is above average, thereby reducing average incomes. Against those who would suggest that aid is in the long-run interests of rich countries, since it averts a potentially explosive situation if the 'gap' becomes very wide, he argues that military interests are not served by helping potential opponents.

His last main theme is the appeal of Marxism in poor countries. He attacks suggestions that little or no progress was or can be made under colonial regimes with examples of rapid progress drawn from West Africa, which he compares with the slow growth in the economies of Ethiopia and Liberia. The return to private capital and the incomes of expatriates are not extracted from others but are payments for services of factors of production. Markets were not 'captured' by the colonising countries since free trade policies were often adopted (e.g., by Great Britain). Marx himself paid tribute (in the Manifesto) to the dynamic potentialities of capitalism in backward societies, and it is the Leninist literature with which Bauer takes special issue as he believes it tries to rescue the unfulfilled predictions of Marx by erecting spurious notions of the capitalist exploitation of poor countries. In his customary exercise of trying to understand how anyone could be attracted by views opposite to his own he says (p. 162) 'Humanitarians and social reformers particularly need people who can be classified plausibly as helpless victims of causes and conditions beyond their control'.

We can summarise the first part of the book on 'Ideology and Experience' and, thereby, Bauer's views as a whole as follows. The arguments of those (notably Myrdal and UNCTAD) who advocate aid and comprehensive planning to break out of the vicious circle of poverty and close the 'gap' are vague, misleading or

wrong. Alternatively, Bauer argues that the primary causes of material advancement are the energy and initiative of the people and that these are best channelled through the free play of market forces unhindered by governments, whether local or foreign. The main role of government should be the supply of a background of services for the proper operation of the market.

The second part of the book, on case studies, is intended to document with examples the views advanced in the first section. The third part contains a collection of review articles and the attacks of the first section are repeated. The attacks take the form of reviews of books containing the opinions under fire and are interspersed with occasional praise of books closer to Bauer's own position.

3. An appraisal

We now turn to a critique of the arguments summarised above. The discussion of each issue follows the pattern outlined in the introduction: the description of the requirements of, and, where possible, a summary of and some conclusions from, a worthwhile analysis of the issue; followed by a comparison with Bauer's offering and, from time to time, some comments on the arguments put by the proponents of the positions Bauer attacks. We examine the topics in the same order as they appear in the summary of Bauer's book.

We deal first, however, with a methodological error which runs through the whole book. The fault lies in Bauer's method of attacking generalisations. When we test a generalisation in the social sciences we are usually trying to tell whether a statement is broadly true and not whether it holds in every case.[2] One is not justified, therefore, in claiming that a generalisation is destroyed by the production of a few counter-examples. It is true that many of those whom Bauer criticises make their claims too categorical, and his criticism of this aspect of their arguments is justified. Bauer talks at some length, however, of the standards of argument required in serious academic discussion. One would have hoped, therefore, that he would have concentrated his analysis on whether the statements under examination were valid in a statistical sense or, if he felt that specific statistical tests were difficult to construct, whether the balance of evidence pointed one way or the other. In the latter case examples can be useful. They must be used, however, in a manner which makes a genuine attempt to balance the evidence. In other words, one should try to straddle the spectrum of possible examples to evaluate whether, and in what ways, the examples being used are representative for the issue under discussion. Ideally one would like a combination of a statistical approach together with the examples. Bauer virtually ignores the first method and misuses the second.

How then might one test the hypothesis of the pervasiveness of vicious circles? Presumably it claims that various factors reinforce each other so that, on the

[2] We are referring to empirical generalisations here rather than theoretical deductions.

whole, the standard-of-living of the poor, or poor countries, tends to grow more slowly than that of the rich. This implies that the dispersion of incomes or wealth in a country and across countries tends to increase or, crudely, the 'gap' tends to widen. It should be emphasised that the widening gap is not the same thing as vicious circles. The former could exist as an empirical phenomenon without the latter being an important explanation. Alternatively, the tendency produced by the phenomenon of vicious circles may be real but be offset by countervailing tendencies. It is a fair test of the *dominance* of vicious circles, however, to ask whether indices of cross-country dispersion of incomes have been increasing. The vicious circle theory is not sufficiently specific for us to identify the precise measure of dispersion which should be used. The data on the international distribution of income are discussed in detail below when we consider the empirical existence, or non-existence, of 'the widening gap'. Anticipating our conclusions, we can say that, at the level of cross-country comparisons of aggregate incomes, the various measures all point in the same direction – that there has been little change[3] in the international distribution of relative income in the last two decades. It appears, therefore, that the vicious circle is not a dominant force at this level for this period.

On a theoretical level the words 'vicious circle' have been used differently by different writers and, at times, differently by the same writer. For example, sometimes it appears that the concept of stable equilibrium (but obviously, for poor countries, at a low level) is being used,[4] sometimes the non-existence of equilibrium and sometimes instability in a downward direction.[5] This confusion has by now rendered the term unhelpful in economic analysis. This does not, of course, imply that all the meanings given to the term, such as that of the low-level equilibrium trap, are useless.

Bauer's contribution to the discussion of vicious circles is minimal. All we are offered by way of testing is one or two examples of countries that have grown relatively rapidly and the claim that the hypothesis is thereby refuted. The analytic criticism Bauer offers is that the hypothesis reduces to the claim that a country is poor because it is poor. This seems reasonable when applied to some forms of the hypothesis, but an analytical discussion should have gone much further – for example, pursuing some of the conceptual issues raised in the previous paragraph. The conclusion, therefore, is that Bauer's attack on the hypothesis of vicious circles is weak, but that the notion itself is imprecise and

[3]This statement depends on the measure but seems justified for many that are commonly used, for example, the Gini coefficient – see below. It should be emphasised that the statement refers to the dispersion of *relative* incomes. Absolute differences appear to be increasing.

Insofar as aid has helped the growth of the poor countries (and lowered the rate for the rich countries) over the period of the data, the effect of vicious circles in the absence of aid is underestimated.

[4]See Nurkse (1953).

[5]See Myrdal (1957) for a discussion which seems to confuse the various notions. He now seems to have committed himself to a definition in terms of cumulative downward motion – see Myrdal (1968, p. 1845).

when taken as implying increasing dispersion of international incomes, unsupported by the evidence.

The next suggestion that comes under criticism from Bauer is that there is an ever-widening 'gap' between rich and poor countries. The testing of such a claim involves the specification of a measure of the 'gap' and the availability of the data which the measure requires.

Kuznets has recently presented an analysis of the ratio of income per capita between rich and poor countries. He shows[6] that (for non-communist countries) the ratio of GDP per capita[7] in developed countries to that in less developed countries has increased from 10.3 in 1950–52 to 11.5 in 1965–67. Developed countries are classified as those with a GDP per capita in 1965 larger than $1,000 together with Japan, although it did not meet this criterion. The rate of growth per capita in developed countries was around 3% and that for less developed around 2% for the same period. There are various reservations about these measures one would want to make, the main one being the classification of Japan. At the beginning of the period Japan had a GDP per capita less than that of Mexico, Panama, and Ireland and similar to that of Greece and Portugal, and at the end of the period a GDP per capita less than that of Venezuela and Libya and similar to that of Ireland and Argentina.[8] All the countries mentioned were classified as less developed and Japan was classified as developed. If Japan had been classified as less developed, the growth rates of the two groups would have been very close.[9]

The international distribution of income has also been studied by Beckerman and Bacon.[10] They construct measures which they feel reflect consumption and GDP of some countries rather better than published national statistics. They examine the change in the international distribution of consumption per capita between 1954–55 and 1962–63. Their measure of inequality is the Gini coefficient

[6]See Kuznets (1972, pp. 40–41).

[7]GNP is preferable to GDP (gross domestic product) as a measure of the income of a country for our purposes. The latter figure refers to the product within the geographical boundary of a country whereas the former refers to the product of factors owned by nationals of the country. GDP is more easily available for large groups of countries and this is the reason it was used by most of the authors quoted. It is unlikely that the above statements would be significantly altered by the use of GNP. One might argue that a measure of the product of factors domestically situated *and* owned would be a better indicator of development than either GNP or GDP.

[8]For the beginning of the period, see U.N. Yearbook of National Accounts Statistics (1962, pp. 314–317) column for 1953. For the end of the period, see U.N. Yearbook of National Accounts Statistics (1969, vol. II, table 1B, pp. 9–14) column for 1965. GDP's per capita in U.S. dollars were not available from this source for 1951 (Kuznets first year) and the 1953 figures for Libya, Venezuela and Argentina are not given.

[9]See table 1.5 in Kuznets (1972), where one example of the effect of the exclusion of Japan from developed countries is to reduce an aggregate measure of rate of growth of income per capita from 3.57% over the period to 2.86% p.a. A complete recalculation of Kuznets' statistic, given the information he provides, would not be easy.

[10]Beckerman and Bacon (1970, pp. 56–74). The only communist countries included were Poland and Yugoslavia.

which they found decreased from 0.570 in 1954–55 to 0.567 in 1962–63 – a change which they, reasonably, judge to be insignificant. The Gini coefficient does have the property that a doubling of everyone's income leaves it unaltered so that it meets Bauer's request to examine relative incomes.[11]

Streissler has recently[12] used a statistic different from that of Beckerman and Bacon to measure dispersion – the variance[13] of the logarithm of per capita GDP. He finds little change from 1953 to 1969.

The recent growth of real GDP per capita of the less developed countries is summarised in the table (see end of paper). The growth rates should be compared with per capita aggregates for developed countries of 2.6 per cent p.a., 1950–52 – 1960–62, and 4.0 per cent p.a., 1960–70.[14] The table illustrates that there is a wide diversity in the recent growth experience of developing countries and, therefore, that examples should be selected cautiously. In this case, an overall statistical approach is both possible (see the studies mentioned) and necessary for the building of a broad picture.

The conclusions from these data would appear to be that over the last twenty years the dispersion of the international distribution of income (measured in terms of the Gini coefficient or the variance of logarithms) has hardly changed. On the other hand, if we split into two groups, developed and less developed, we find that the countries in the former have grown (in per capita terms[15]) a little faster. This is not contradictory since the difference in growth rates is fairly small, dispersion inside the two groups may have increased and, as already noted, the classification of Japan as developed for the relevant period is debatable and has a significant effect on the comparison. In my view, the overall measure of dispersion is preferable to a simple comparison of the behaviour of two sub-groups for the question at hand. The split into two sub-groups is bound to be somewhat arbitrary and movements *inside* the sub-groups are obscured. Naturally, the overall measure should be supplemented with the examination of examples.

It seems, then, that the data do not lend strong support to the notion of a widening gap. Bauer's discussion of these data, however, has added little constructive to the analysis of the 'widening gap'. He has offered a few examples of rapid growth and complained that previous analyses have not been in terms of ratios of income per head when the data for such an approach were readily available.[16] One is prepared to share his caution over the accuracy of the data, but at present they are all we have. In measuring the above changes we do not

[11]Various indices of inequality, including the Gini coefficient, are discussed and compared in Atkinson (1970, pp. 244–263).

[12]Seminar paper at Oxford (Spring, 1973). The communist countries were excluded.

[13]This statistic also has the property that it is unchanged if all incomes are, e.g., doubled.

[14]See Kuznets (1972) and U.N. Yearbook of National Accounts Statistics (1971).

[15]Total GDP in less developed countries has grown faster than in the developed but this has been offset by higher population growth – see Kuznets (1972, p. 20).

[16]U.N. Statistical Year Book, for example, has been published since 1948 and Kuznets' detailed discussion of historical statistics *Modern economic growth* was published in 1966.

require that biases are absent but that they are constant. Further, Bauer himself is prepared to use these data for his occasional examples.

The data on national incomes are much better after the Second World War and the above discussion, therefore, concentrated on this period. Some of those Bauer criticises were, however, referring to much longer periods.[17] Kuznets (1972, p. 19) suggests 'A reasonable conjecture is that, in comparison with the quintupling of the per capita product of developed countries over the last century, the per capita product of the 'poor' LDC's rose two-thirds at most: and that this relation would hold roughly, even if we were to measure the century back from 1965 (rather than from the mid-1950's)'. Even though the data are poor, the indications are that the statistical measures discussed above would show big increases between the 1850's and 1950's. It must be admitted that the authors cited by Bauer[18] were vague but it is rather unfair to pick a few observations from a period after the one they were discussing.

It should be noted that all three studies quoted above have been in terms of ratios of income per head, as Bauer would want. If the 'gap' in relative incomes has remained constant, that in absolute incomes has increased. It is currently fashionable to use indices that indicate dispersion in relative incomes – in other words, if we double everyone's income the index of inequality remains unchanged.[19] Suppose, for example, we have a community of two men, A with one unit and B with a 100 units. If we give A one unit and B 100 units, then the above inequality measures remain unchanged. Some would want to say inequality has increased. Bauer offers examples, which have some appeal (p. 51), that suggest that relative income levels *are* the appropriate arguments for the indices. The issue is much more open than Bauer grants – it is an ethical question and there is no monopoly on the truth.

I share Bauer's concern, however, with the level of aggregation involved in the split into two big sub-groups – developed and less developed. He complains that the slow growth of some poor countries masks the rapid growth of others when we aggregate. Others might put the emphasis the other way. They would be concerned that the statement that the gap has not widened might mask the fact that some poor countries have been growing very slowly. We return to this point and to the relevance of the precise magnitude of the 'gap' when we discuss aid.

In analysing Bauer's views on central planning we should be clear that his attack does not involve a demand for total inactivity on the part of the government. He outlines (pp. 90–91) the following governmental tasks: management of external affairs, maintenance of law and order, monetary and fiscal policy, 'promotion of a suitable framework for the activities of individuals, basic health and education services, basic communications and agricultural extension work'.

[17] Myrdal (1956), which Bauer criticises in (1971, pp. 452–453), cites H. Singer (1949) who was clearly referring to the first fifty years of this century.

[18] See previous footnote.

[19] See Atkinson (1970).

He claims that, 'This list of tasks largely exhausts the potentialities of state action in the promotion of general living standards'. Bauer believes that activities which are not seen as profitable by groups or individuals within the framework he describes should not be undertaken since it is unlikely that they will be worthwhile. These views, summarised in 2 above, are based on a generalised mistrust of bureaucracies as against individuals operating directly in their own interests, and the results of economic theory concerning the way in which competitive markets allocate resources.

Bauer has pointed to some of the problems of planning and government intervention in a clear and incisive way. He fails, however, to give an adequate account of the problems of market power and seems unaware, or deliberately ignorant, of those results in economic theory which clarify the (numerous) circumstances in which the market can be inefficient. Our discussion of Bauer's restricted view of appropriate areas for government activity, whilst accepting some of Bauer's points about bureaucracies and government power, is intended to redress the balance by pointing to the problems of the market. This discussion is introduced with an example of a valuable government-sponsored project which would not have been pursued by private enterprise. This is not intended, by itself, as a destruction of Bauer's argument but as an indication of the *issues* that are involved in an analysis of the appropriate degree of government intervention. Many of the points raised by the example are general. Bauer's contribution can then be put into perspective.

In 1961, a Special Crops Development Authority was established in Kenya to encourage the development of tea on peasant small-holdings. In 1964, this became the Kenya Tea Development Authority (KTDA). Previously tea in Kenya (and most of the world) had been entirely an estate crop. The operation involved careful organisation by the KTDA. Education in tea culture for the farmers, establishment of special factories, and loan and credit facilities were all necessary in a carefully integrated exercise. The whole operation was very successful and in its first decade 60,000 acres of small-holder tea were established. Standards were high and the tea produced on small-holdings obtained good prices in London.

It is very unlikely that this operation would have occurred without aid and government intervention. Private tea factories did not have confidence in the skill of peasant growers in the absence of government backing and training. The factories had existed in Kenya since before the Second World War without there being any important approach to peasant growers. The growers themselves would have suspected factories of exploiting them if government supervision had been lacking. Indeed, as sole buyer (plucked tea must be processed within a few hours) the local factory would have been in a very powerful position.[20]

[20]In Java the factory–peasant suspicion and hostility was an important reason for the failure of a tea scheme; see McWilliam (1957).

The private capital market would not have given loans to growers to keep up their consumption levels during the long gestation period. The organisational costs of arranging and supervising each loan would have been unprofitable. These costs were much less for the government as it was already organising the sale of the produce and looking after accounts of each grower.

The advantage of small-holdings over estates in this case was that tea benefits from careful, attentive husbandry. With good farmers this was more likely to be forthcoming from the small-holder organising the labour himself, with greater flexibility, lower cost and greater concentration. There are possible offsetting disadvantages, of course, but in this case the structure was such that a successful combination of small-scale (individual tea gardens) and large-scale (collection, processing and sale) was obtained. The project was a good one without counting any spin-off effects but doubtless Bauer would approve of the stimulus to entrepreneurship promoted by the successful introduction of a new cash crop.

This is just one example of a situation in which there was a profitable opportunity which was unlikely to be taken by private enterprise, for the reasons outlined, but was suitable for government action. The precise combination of ingredients in the example may not be repeated elsewhere but there are individual elements which are common and by themselves can cause the price mechanism to fail to bring about the exploitation of worthwhile opportunities. It is well-known that the existence of increasing returns to scale in production is incompatible with perfect competition, and that there is no special reason to expect the private alternatives to perfect competition to lead to beneficial outcomes. Loan markets are often imperfect or non-existent if borrower and lender take a different view of the likely risk of a project. Transaction costs of arranging loans and projects will often be cheaper for the government than private enterprise. Debt collection may be easier for governments. Risk-pooling can be achieved at a government level but might not be possible at a smaller scale. Bauer might argue that in these cases private enterprise could operate on a large scale too, but we have already pointed out that there are problems associated with the market power of these large scale private enterprises.

There are other reasons why market prices might not reflect the opportunity cost of resources. The tax tools available to the government may be limited so that it may have to impose commodity taxes. Prices of goods will not necessarily reflect opportunity costs if the inputs to those goods are inappropriately priced owing, for example, to monopoly, market failure or taxes. There may be significant externalities from the use of inputs and outputs which are such that an appropriate corrective tax or subsidy is very difficult to implement.

Another important problem with a total reliance on the price mechanism is that a distribution of income might be generated which the government finds undesirable but which it can change only at some cost of resources. Thus, the case for government intervention will depend, in part, on its objectives as regards income distribution. If a government attaches a high priority to raising the

incomes of the poorest section of the community,[21] and the price mechanism leads to little or no growth in these incomes, then government intervention may be seen as desirable. There may also be objectives distinct from the size of national income and its distribution. For example, a desire for collective decision-making will have consequences for views on decentralization through the price mechanism. These alternative objectives are perfectly legitimate, have implications for government intervention and are ignored by Bauer.

The example of the tea scheme and the worries about the price mechanism are offered to show that there are serious objections to Bauer's request to leave everything outside his list to private enterprise. There are, naturally, problems associated with comprehensive planning, some of which Bauer mentions and which have been described above. Some of his objections are invalid, however. For example, he suggests (p. 86), 'Comprehensive planning implies further that much of output is unrelated to consumer demand and, therefore, to living standards'. There is nothing inherent in planning that implies this claim is true. Indeed, if used to help overcome some of the difficulties of the price mechanism it can make output *more* responsive to consumer demands. Whether or not planning and government intervention actually will produce improvements when the market is defective is a matter of judgement and analysis in any situation.

Another problem with Bauer's claim that planning produces output unrelated to consumer demand is his insistence (e.g., pp. 69–95) on the importance of personal attitudes and aptitudes in determining material progress. If attitudes and preferences change during the development process, it is problematic which set of attitudes one should take as defining consumer demand.[22]

A similar problem is concerned with the preferences of future generations. One can argue that individual saving decisions take insufficient account of future generations and that the government should feel a duty to consider the demands of future generations. Sen[23] has shown that the answer to this philosophical question depends, inter alia, on the individual's relative valuation of his own consumption, that of his heirs, his contemporaries and their heirs, as well as his assumptions on the distribution of the benefits of his saving between his own heirs and those of his contemporaries. Further, the relative valuations of consumption now and consumption of heirs depend on an estimate of the rate of growth of consumption, which may well be a difficult decision for an individual. The whole question of the appropriate rate of saving is a tricky one and it is certainly not obvious that preferences as reflected in free markets have an overwhelming priority.

The appropriate division of the economy into public and private sectors is a subtle and complex issue as is the desirable degree of intervention in markets. There are a few general statements one might want to make, however. For

[21] See the essay by Bhagwati and Pant in J. Bhagwati (197..).

[22] For example, individuals may be resistant to a certain form of education but ex post be rather pleased that they were educated that way.

[23] See Sen (1967).

example, the insurance markets and capital markets may be particularly suited to government intervention (see the above comments on the tea scheme). Weitzman[24] has recently offered a discussion of the situations when the price mechanism is preferable to fixed quotas and vice-versa. Further, one should not minimise the political and social problems of changing the degree of government intervention. One may have to attack considerable vested interests or take great care with the types of interest one is creating. This is not the place to pursue such an analysis. The intention is merely to point out that analysis of these questions is possible, that it is not usually easy and that answers will depend on particular situations. Bauer offers a one-sided and facile account of an important problem. It is no excuse that those he criticises offer arguments that are equally facile and one-sided.

Bauer's attacks on Marxist writers on development will not be analysed in detail here. There is one of Bauer's claims, however, which is difficult to ignore, is central to his argument and is given insufficient justification. Bauer states (p. 169), 'When such (dividend and interest) payments occur they represent returns on resources supplied from abroad and not payments extracted from the local population'. The generality of this claim cannot be sustained.

Let us take the case of a foreign company extracting minerals. The profits of the mining companies can be regarded partly as a rent resulting from the right to exploit the resource and partly as a payment for the capital services required to obtain the minerals. If we regard, as seems reasonable, the natural resource as belonging to the country in which it is found, then the rent element of the profits should go to the country.

The calculation of the rent element is complicated. The most a mining company beginning exploration on a piece of land would be prepared to pay for that land is the expected profit from its activities (discounted over the future) less the expected profit it could have obtained from use of its resources elsewhere (for example, investing its capital in some fixed interest market).[25] The calculation of expected profit from its activities should include the possibility that no or few minerals will be found on the land, and the possibility of future expropriation. Let us call the most the company would pay, as defined above, the value of the land. This value is the worth of the right to exploit the resource and, on our definition of the appropriate rent, this value should be equal to the discounted sum of the rents.

Putting the argument another way, we can say that Bauer, in order to justify his claim that profits are the return to resources supplied, would have to show

[24] MIT Economics Department Working Paper no. 106. His result is that, in an uncertain situation, the price mechanism may be an inappropriate tool where marginal costs are (nearly) constant and marginal benefits vary sharply with output. A small error in marginal cost may lead to a big change in the quantity decision (if the rule is price equals marginal cost) with, possibly, damaging effects on benefits.

[25] We are assuming the firm is risk-neutral and we are, for expositional purposes, subtracting expected profit elsewhere rather than netting out capital costs from the time stream.

that the firm has paid (or is paying) through the purchase price of the land (or rents and profits taxes) the value of the land as defined above. This exercise would involve a considerable amount of work and presumably the answer would vary from case to case. Bauer does not offer any evidence,[26] and in the absence of this there is no special reason to believe that the examples where the proper price (or too high a price) for the land was paid outnumber those where the land, or development rights, were acquired at a price that was nominal or too low. Indeed, there is reason to suppose many prices were too low; for example, in cases where the rights to exploit the minerals were granted by colonial governments, or acquired by corrupt practices (e.g., bribing of officials) or where offered prices for the rights were suppressed by monopoly practices of groups of companies.

Many of the less developed countries have realised that they have genuine claims against the assets of some foreign companies for this reason, and are now reaping the fruits of the exercise of these claims.

Bauer himself has his own broad generalisation – that the energy and initiative of groups and individuals, channelled through the market mechanism, are the most important determinants of material progress. It is very difficult to examine this proposition. Examples of rapid output growth under strict planning, such as the U.S.S.R. after 1917, would not constitute a sufficient counter-argument since Bauer could legitimately claim that the growth in consumption was much slower than that of output and it is hard to tell what would have happened in the absence of planning. Further, the production of a few counter-examples would be to use Bauer's own mode of argument which we have just criticised. The main difficulty, however, would be in deriving a definition of initiative which did not automatically give results which supported Bauer's thesis. The reason is that most practical measures of initiative would be based on success of some kind, while we are concerned with the proposition that initiative brings success. Whether or not such a claim is, in principle, testable, Bauer himself does not offer proper justification. It is an example of the difference between the standards he applies to his own arguments and those he would like to apply to others.

4. The arguments for aid

The main argument for aid[27] is as a transfer from the better-off to the worse-off which is of sufficient benefit to the latter to justify the cost to the former. In order to use this argument we must outline the moral principles on which the

[26]The only historical calculation of this kind of which I am aware is that of Frankel (1967) in his discussion of the South African gold mining industry. He found similar rates of return to other comparable areas of international investment but these were higher than for U.K. equities.

[27]The term 'aid' is taken here to mean (non-military) grants from official bodies and from charities. 'Soft' loans can be converted to grant-equivalents and included in the total by subtracting from the initial sum the net flow of interest and amortization payments discounted at the market rate of interest.

claim is made, and which clarify the notion of 'sufficient',[28] and show that the conditions for the argument are, or can be, satisfied by aid.

We first show that the aid can be a transfer from the better-off to the worse-off. The difference in incomes between some developed and less developed countries is huge. For example, the GNP per capita in India and Indonesia in U.S. dollars in 1969 was 86 and 81, respectively. These figures can be compared with 1969 levels in the U.K. and U.S.A. of 1823 and 4139 dollars, respectively. The growth rates of GNP per capita in the first two countries from 1960–1970 were less than 1%, whereas those for the U.K. and U.S.A. were 2.2% and 3.0%.[29]

It is these facts which should have more direct impact on the arguments for aid than aggregate measures of 'the gap', and which indicate that the case for aid to these countries is growing stronger whether or not some measure of the dispersion in world incomes has increased. The difference in incomes is sufficiently large that errors in the measurement of GNP are unlikely to be relevant to the general picture.[30] Bauer, although understandably sceptical about national income statistics, would surely agree that the U.S.A. is much richer than India.

The magnitude of the difference implies that a relatively small sacrifice to a rich country constitutes a relatively large addition to the income of a poor country. If we give 1% of our GNP to a country with the same population and 1/20 of our income then their income is increased by 20%. If, for example, half of this increase is devoted to investment this might be a doubling of their investment programme. The case for a transfer from the rich in rich countries to the poor in poor countries is even stronger than is suggested by average figures since the difference in their income levels is, of course, much larger than the difference between the average incomes. Through official and progressive tax systems in rich countries and careful allocation in poor countries, such transfers are possible, as they are through voluntary aid organisations. When announcing in 1973 the World Bank's re-orientation of priorities towards alleviating rural poverty, McNamara (1973, p. 13) said, 'Within the rural areas the poverty problem revolves primarily around the low productivity of the millions of small subsistence farms. The truth is that, despite all the growth of the GNP, the increase in the productivity of these small family farms in the last decade has been so small as to be virtually imperceptible'. It is suggested that this statement is relevant for a large proportion (up to 40%) of the population of many poor countries.

[28] Some might wish to be explicit that the aid be used for investment rather than consumption purposes or that the possibility of graft is minimal. I have no wish to be dogmatic on the former point, and if the potential benefit is large, one might be prepared to accept a small probability of graft if this were unavoidable. Both issues can be subsumed under 'sufficient benefit'.

[29] The U.N. Statistical Yearbook (1972, tables 185 and 187).

[30] Bauer (pp. 57-58) leans heavily on Usher (1968) for support of his view that current GDP comparisons have little meaning. However, Usher's recalculations for U.K. and Thailand, while narrowing the gap considerably, still leave large income differences (over 3 : 1 in 1963). Further, Kuznets (1966, p. 375 and Table 7.3) had previously performed revisions of the Usher type and suggested (p. 386), for example, that the *lowest reasonable* estimate of the ratio of U.S.A. to Asian product per capita in 1958 was 8.7 : 1.

The existence of a progressive tax system in many developed countries, together with the increasing concern of aid agencies towards the problems of the poor in poor countries and the massive difference in the average incomes of some rich and poor countries is surely sufficient evidence to show that aid can be, and much is, a transfer from the wealthy to the very poor.

To show that aid can be beneficial we could produce a long list of valuable projects from the experience of private aid agencies such as Oxfam or public bodies such as the World Bank which would follow on from the example of the tea scheme described earlier, and which would not have taken place without aid. We offer just five examples of successful aid projects to add to the Kenyan tea project already mentioned. The first is the Vuvulane sugar scheme in Swaziland. The U.K. government Commonwealth Development Corporation financed the irrigation of land which was let on long leases to Swazi farmers. The farmers devote most of their land to sugar which is processed in a nearby mill. There is great enthusiasm amongst growers for the crop and it has been a real encouragement to peasant cash crops in Swaziland.[31] Both Hirschman and King[32] in their recent books on World Bank financed projects point to the El Salvador Lenga River Hydroelectric Scheme and the Chao Phya River Irrigation Scheme in Thailand as successful projects. On a much smaller scale, but still of importance, are the activities of voluntary development and relief organisations such as Oxfam. Just two examples of Oxfam projects are offered here. A great many more are possible. In Khadigram, Bihar Oxfam funded a centre for agricultural extension which instructs farmers in the use of fertilisers, better cultivation methods and newer varieties of crops. Oxfam granted finance for the equipment of a machine shop for the technical training of poor boys in Don Bosco School, Liluah, Calcutta.[33]

The agencies involved in the examples range from a single government organisation (U.K. government C.D.C.) to the World Bank and a charity, Oxfam. The countries involved, from El Salvador to India. The list could, of course, be extended. These examples cannot *prove* that success can be guaranteed. They are offered to suggest that careful search and selection can yield projects with a reasonable chance of producing net benefits; and this is sufficient for the moral argument to stand. There is some cross-country statistical evidence [see Papanek (1973)] which also supports the view that aid is productive. This is discussed later when we look at Bauer's alleged harmful effects of aid.

We are supposing above that the aid resulted in a genuine increase in the investment budget. In other words, we are assuming that the domestic supply of investible funds was reduced by less than the aid. For example, one would guess that the post-war growth of Israel and Taiwan was greater than it would have been with less aid. Mason, in his comparison of the experiences of India and Pakistan, suggested that Pakistan's higher level of aid per capita made industrial

[31] This project was visited by the author in 1974.

[32] Hirschman (1967), King (1967).

[33] For further details, see Gill (1970).

development substantially easier than in India.[34] A positive relation between investment and aid for all countries is not something that one can prove, and again we have to make a judgement based on evidence. We return to such empirical studies later but it is hard to avoid being suspicious of arguments of the kind 'more from outside means less altogether'. Further, for the moral argument we are using we need not insist that aid is invested.

There is a reasonable hope that, as methods of project identification and management improve and the lessons of previous projects are digested, aid will increase in effectiveness over time. One must avoid blind faith in the onward march of reason and doubtlessly mistakes will continue and relapses occur, but over the last decade techniques have improved[35] and ex-post analyses of aid-financed projects carried out.[36]

We deal with some of the alleged deleterious effects of aid when we discuss Bauer's arguments specifically. We have suggested, then, that with careful allocation, aid can be beneficial to poor countries. This means that project-aid or aid with appropriate strings attached may often be desirable. There are political limits, however, to the extent to which outside bodies can dictate the way in which aid is spent and we should not forget that recipient countries themselves will often be the best judges of their own interests.

A small sacrifice on the part of rich countries can, therefore, produce a probability of benefits to the poor yielding an expected benefit sufficiently large to provide a moral justification for many prospective donors. In practice, it should not be too difficult to provide evidence on both empirical parts of this statement, in other words, to determine the relative wealth of donors and beneficiaries and to examine the effectiveness of possible uses of the aid.

For many this would constitute sufficient evidence to justify the sacrifice. There are various moral positions from which such a conclusion could be drawn; for example, the utilitarian, a preference for equality per se, or Rawls'[37] notion of justice. It may simply be a desire to help others[38] which is not necessarily articulated in terms of any particular system of ethics. This is not the place for a lengthy discussion of this conclusion or the moral positions. The conclusion, however, is one that many would accept.

There are other arguments for aid, which run in terms of the self-interest of the rich countries, which have somewhat less importance, in my view, but which might seem more attractive to others. For example, one could argue that aid helps stimulate other poorer economies and that, in the long run, healthy

[34] Mason (1966, p. 64). Brecher and Abbas (1972, p. 163) state that, 'Expansion of Pakistan industry and of the economy as a whole, would have been severely restricted and retarded by a forced heavier reliance on domestic resources'.

[35] On appraisal useful manuals of social cost–benefit analysis have already been published by the OECD Development Centre and UNIDO. Similar manuals are in preparation at the World Bank and the British ODA.

[36] Hirschman (1967) and King (1967).

[37] Rawls (1972).

[38] Or to help them help themselves.

trading partners are important as markets both for the purchase of our inputs and the sale of our outputs. Alternatively, and rather less attractive as a moral position, one might argue that recipient countries will look more favourably on the interests of major donors than on those developed countries which give little. Detailed theoretical and empirical justification is needed for the assumptions underlying these arguments.

Having stated the case for aid we are in a position to evaluate the importance of Bauer's arguments. Bauer claims that aid leads to the transfer of inappropriate institutions and attitudes from donor countries or to misguided policies in general. There is nothing inherent in aid per se that implies that the recipient country builds foreign-style universities, indulges in comprehensive planning, totally ignores balance-of-payments constraints or pursues any other policy which Bauer regards as unattractive.

Indeed, aid has recently come under criticism from the far Left[39] on the grounds that it leads to pressure for laissez-faire, rigid monetary control and lower taxes on capitalists; in other words, policies some of which Bauer would advocate. It is clear that the claims of both sides cannot be right, either as generalisations or in a particular case. Neither side gives convincing arguments that the pressure will usually be, or has usually been, in the direction it describes. In the absence of a demonstration that aid must lead to pressure for damaging policies, the discussion of aid should lead away from attacks on aid itself and towards an examination of the types of aid that are desirable.

Bauer's contention that aid may reduce thriftiness or is more likely to be squandered than domestic savings is not supported by empirical analysis. Bauer himself offers no such analysis, but the subject of saving in developing countries has recently been surveyed by Mikesell and Zinser.[40] They report that there is a negative correlation between capital inflows and domestic saving rate across countries. This, of course, does not imply that countries save less (out of total new resources–domestic production plus capital inflow) when they receive extra capital from outside. If total saving increases, but by less than the total inflow, then some of the extra has been saved and some consumed even though *domestic* saving (i.e., output less consumption) decreases.[41] There is the possibility that more aid is allocated to poorer countries and that those are the countries which

[39]Hayter (1971).

[40]Mikesell and Zinser, (1973, pp. 1–26). See also Griffin (1970) and the comments and reply (1971).

[41]To quote from Mikesell and Zinser, 'This situation is well illustrated by the case of Israel during the 1950's when, as a consequence of very large capital inflows, measured net saving for the economy was slightly negative. Yet family savings surveys of Israel's economy showed positive saving out of disposable income (which included some capital inflow items) to be nearly six per cent' (1973, p. 15). We can put the argument more formally as follows. If we consider the reduced form of a simultaneous equations model of an economy with domestic savings as endogenous and capital inflow as exogenous, then an increase in capital inflow increases total savings if the coefficient on capital inflow in the domestic savings equation is greater than minus one.

save less.[42] This could also explain the negative correlation. Further, for the purposes of these regressions capital inflow is taken to be current foreign deficit. Both Stewart and Lipton[43] have shown that this can be misleading. Low saving may cause a balance of payments deficit if it is insufficient to meet investment. An excellent survey and critique of the work relating domestic savings and foreign aid is contained in Lipton (1972).

Bauer offers no evidence that aid is more likely to be squandered than domestic saving. Indeed, the available evidence is to the contrary. Papanek (1973) finds in his cross-country analysis of growth rates that the contribution of foreign aid is more significant than that of domestic saving (having a higher coefficient). Mikesell and Zinser (1973) report a study by Strout with a similar conclusion.

Good further discussions of savings and aid are available in the papers by Lipton, Mikesell and Zinser, and Papanek. All provide careful appraisals of existing literature and data in a way that Bauer does not and all come to conclusions opposite Bauer's own.

Bauer's claim that good projects, if they really are good, can raise loans without aid is clearly wrong in the light of what has already been said on the efficiency of capital markets in some poor countries and the possible existence of signals from the price mechanism which are misleading. Further, there may be many projects, such as the control of water resources, which can be highly beneficial but whose benefits are such that any financial return is costly or impossible to recoup directly.[44] These projects may find it very difficult to obtain loan support on the private capital market. Further, the suggestion that a loan could be raised for a project if aid were not provided is irrelevant if one accepts our main argument for aid.

Bauer is wrong to suggest that the giving of aid is an acknowledgement of the historical responsibility of the rich countries for the poverty of the poor since we have seen that the argument for aid does not depend on the assertion of such a responsibility. On the other hand, he argues convincingly (and in my view, correctly) that in many cases the poverty of the poor countries (for example, the most isolated) was not caused by the rich.

Bauer is similarly confused when he questions poverty as a criterion for aid by asking whether the expulsion of richer members of the population constitutes an argument for aid. The suggestion that poverty is part of the criterion does not involve the claim that it is the whole story and cannot be outweighed in the argument by the policies of recipient countries.

[42]This supposition is supported by the empirical work of Papanek (1973). Similarly high aid and low saving may occur together with a natural disaster.

[43]Stewart (1971) and Lipton (1972).

[44]The costs may be the distortions that would be involved in the use of the available tax structure or from charging a price higher than the government would otherwise view as correct. Naturally, one needs to take into account the appropriate value on public funds when deciding whether or not to make a loss. Effects on future credit-worthiness may be relevant here.

In fairness to Bauer, we should mention that he does not see his arguments as constituting a case for no aid at all, although he sometimes gives that impression. He sets out (p. 134) various criteria that aid should satisfy. It should favour governments that 'try to govern rather than to plan'. Preference should be given to governments interested in improving, for example, roads and external contacts. Third, aid should be untied in the sense that exporters from donor countries are not subsidised, and bilateral (so that there is proper scrutiny). In other words, Bauer too is in favour of, what he sees to be, 'good' aid.

We are left with the conclusion that the case for aid remains very strong. Bauer regards his conditions for aid as conducive to material progress but we have seen that much of Bauer's analysis in support of these conditions is unconvincing. There are other criteria, however, some of which have been mentioned in the course of the review. This is not the place for a detailed discussion of these criteria, but they would come under two main headings: criteria for, first, project-tied aid and second, aid direct to governments. Where aid is project-tied the worth of the project should be carefully scrutinised, taking into account the relative incomes of those who receive benefits and bear costs.[45]

Where aid is direct to governments the criteria are less definite. This does not mean that they do not exist; for example, one might wish to avoid giving aid to governments that persecuted substantial sections of the population, or used it to buy arms for belligerent purposes, or indulged in massive prestige projects of dubious value. Ceteris paribus, the poorer countries should have priority. Over-rigidity of criteria is to be avoided, however, as there is no unambiguously best way to develop. Further, criteria developed entirely externally may be inappropriate and dictation may be (understandably) resented by recipient countries.

The determination of appropriate methods of allocation of aid is a problem that clearly interests Bauer, and is one that requires more work. Further, his own experience with developing countries makes him well qualified to participate in this work. It is to be hoped, therefore, that Bauer will turn his energies towards these more positive aspects of the discussion of aid and away from creating the impression that aid, per se, is bad.

5. Concluding remarks

Dissent on development is not a valuable contribution to the study of development. Some of the positions Bauer himself takes are sustainable, others are difficult to justify, but in most cases his analysis in support of them is superficial. Many of the statements and arguments that Bauer attacks are weak but, unfortunately, he usually makes a poor job of their destruction. The analytic failings of Bauer's offering are all the more regrettable since some of his early work, on West African Trade, for example, is of lasting value.

[45] Some of the available techniques were mentioned in footnote 35.

Table 1

Recent growth of selected developing countries; average rates of growth of real GDP, population and real GDP per capita in per cent p.a.[a]

	1950–52 to 1957–59			1960–70		
	Gross Domestic Product	Population	GDP per Head	Gross Domestic Product	Population	GDP per Head
Six largest countries						
India	3.3	1.9	1.3	4.0	2.5	1.4
Indonesia	n.a.	2.1	n.a.	3.2	2.6	0.6
Pakistan (incl. Bangladesh)	2.5	2.3	0.2	5.5	2.2	3.2
Brazil	5.5	3.3	2.1	6.1	3.2	2.8
Nigeria	3.7	1.9	1.7	2.9	2.5	0.4
Mexico	6.1	3.2	2.9	7.2	3.5	3.6
Four fastest growing countries[b]						
1950–52 to 1957–59						
Jamaica	10.1	1.6	8.4			
Iraq	10.6	2.9	7.5			
Israel	10.1	4.6	5.3			
Venezuela	8.4	4.1	4.2			
1960–70						
Libya				19.5	3.7	15.2
Hong Kong				12.9	3.0	9.7
S. Korea				10.7	2.6	7.9
Saudi Arabia				9.8	2.6	7.0
Four slowest growing countries[b]						
1950–52 to 1957–59						
Bolivia	−1.1	1.4	−2.4			
Morocco	1.4	2.7	−1.3			
Haiti	1.5	1.7	−0.2			
Pakistan	2.5	2.3	0.2			
1960–70						
Chad[c]				−1.8	2.2	−3.9
Haiti				0.6	2.0	−1.4
Senegal[c]				1.2	2.4	−1.2
Guinea[c]				2.1	2.5	−0.4

[a] These figures are taken from a table prepared by M. Dowley for lectures by I.M.D. Little in Oxford University, 1973. I am very grateful to Professor Little for making these statistics available.

[b] Countries with population less than 1 million are excluded from this section of the table.

[c] Not shown separately in 1950–52 to 1957–59.

Sources: OECD Development Centre – National accounts of less developed countries 1950–66 and 1959–68.
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