Global Integration in Pursuit of Sustainable Human Development : Analytical Perspectives

Manuel R. Agosin and David E. Bloom

I. Introduction

In the closing years of the twentieth century, most developing countries adopted increasingly liberal strategies of economic development. They opened domestic markets to international trade, gave market forces greater play in the allocation of resources, and privatized many state-owned enterprises. There was also a sea change in policies towards foreign direct investment (FDI), with liberalizing measures far exceeding restrictive ones throughout the 1990s (UNCTAD, 2000).

However, liberalization has not delivered the expected rates of economic growth and the gap between rich and poor countries has continued to grow. According to the World Bank (1999), between 1985 and 1997, more than half of the poor countries fell further behind the world leader (the United States), while fewer than a quarter made significant gains. The output gap is measured in terms of the ratio of a country's per capita GDP, measured in units of equivalent purchasing power (PPP), to that of the United States. Data are available for 100 countries, of whom 54 saw an increasing gap, 22 a decreasing one.

The breakdown of the World Trade Organization (WTO) meeting in Seattle has crystallized concerns about the direction of globalization, among both proponents and opponents. Strongly liberal voices such as *The Economist* described the breakdown as "a global disaster" and claimed, "the poor will be the real losers".[1] Others welcomed what they saw as the humbling of the WTO, arguing that "globalization is hurting too many and helping too few", and that "the forces behind global economic change – which exalt deregulation, cater to corporations, undermine social structures, and ignore popular concerns – cannot be sustained."[2] Meanwhile Claude Smadja, Managing Director of the World Economic Forum, has warned of the danger of a backlash against globalization,

[1] See various articles in *The Economist*, 11 December 1999.
[2] Jay Mazur, "Labour's new internationalism", *Foreign Affairs*, January/February 2000. Jay Mazur is Chair of the American Foundation of Labour and Congress of Industrial Organizations (AFL-CIO) International Affairs Committee, as well as President of the Union of Needletrade, Industrial, and Textile Employees.

which “may put at risk the benefits that globalization has brought to both the developed world and the emerging-market economies”.[3]

Surprisingly, there is some agreement amongst these very different commentators about the direction that should now be taken. Jay Mazur argues against building “walls against the world economy”, but calls instead for “an effort to build rules into it, and a floor under it.” *The Economist* admits that neither trade nor globalization in general will be sufficient to give the photogenic Indian girl pictured on its cover a better life, and that “above all she needs education, health, and much else.” Claude Smadja heralds the death of the “triumphalist thesis of globalization”, where globalization is conceived purely in economic terms and dictated by the “pace, modalities, and agenda” of the industrialized countries.

From a developing country perspective, it is now clear that a “*passive* policy” of liberalization is no longer sufficient and that a range of “*active* policies” is needed (see chapter 3 of this book). From an economic perspective, these policies recognize that liberalization offers economies *opportunities*. These opportunities will only be successfully exploited if sufficient capacity is developed to enable a range of actors to engage successfully with the new market conditions. Furthermore, a broader perspective reminds us that economic growth is only a means to the more significant goal of human and social development. Human capital, social capital and economic growth are all intricately bound in a series of complex relationships. Each has the potential to support the other, but equally deficits in one area can lead to deterioration in the others. Virtuous and vicious spirals are therefore possible, indicating the necessity for a balanced approach to development, although there is some evidence that a policy environment that emphasizes human development is more likely to lead to a *virtuous spiral* than one that stresses economic growth.

This paper discusses three complementary policy spheres, covering:

- Integration into the global economy and liberalization of markets
- The promotion of fast economic growth
- Sustainable human development (SHD)

---

[3] Claude Smadja, “Time To Learn From Seattle”, *Newsweek International*, January 17, 2000.

The three policy spheres can be characterized as intersecting circles (see figure 2.1). Confining policy initiatives to a single sphere tends to deliver disappointing results. Sustained development (economic, human, and social) is most likely to be achieved at the intersection of the three spheres. Democratic governments must therefore develop a balanced policy portfolio, at the same time commanding electoral support and likely to contribute to the development of virtuous spirals of development. They must be aware of the extent of their power to promote change in any area, and of the possibility that government intervention may inhibit action by other actors. In many cases, civil society and the business sector may be able to play a significant and increasing role in promoting broad-based development.

[Insert figure 2.1]

For aid organizations (operating at national or international levels) and other multi-lateral actors, there is a strong case for a more broad-based approach to providing development assistance. The World Bank, for example, has come up with its Comprehensive Development Framework, which aims to promote partnership between different institutions and maintain progress along a number of fronts. There are still unanswered questions about whether this approach will increase the effectiveness of development assistance and how to reconcile the agendas of different national and multinational actors. Nevertheless, there is now a growing body of evidence and analysis available to policymakers seeking to develop a context in which liberalization and globalization deliver enhanced benefits to people while simultaneously ameliorating some of the harsher impacts of these processes.

II. The Three Spheres

Sphere 1: Integration into the global economy

For most developing countries, openness to the international economy provides the best environment for stimulating growth. Many developing countries are small, and inward-looking economic strategies can therefore quickly come up against demand constraints. Countries that export are able to grow much faster, especially if they can diversify the products they bring to international markets. Openness, of course, is a two-way process.

Export earnings allow increased investment in imported capital equipment, which combines capital accumulation with access to modern technologies to improve productivity. At a time when markets are developing so fast, closed economies are becoming ever less viable.

To achieve openness, developing countries have adopted a number of policies:

- *Trade liberalization* – most developing countries have significantly lowered their trade barriers, with average tariff levels down, and tariff dispersion narrowed considerably. Countries joining the WTO, in line with their new international obligations, have dismantled a variety of subsidies and non-tariff barriers to trade. Many countries have also signed free trade agreements with neighbors and occasionally with developed countries.
- *Liberalization of FDI* – most developing countries have liberalized their FDI regimes. Indeed, some now have FDI regimes that are distinctly more liberal than those in the developed world (Agosin, 1999).
- *Freeing of non-FDI capital flows* – many developing countries now look to international financial markets to supplement investment from domestic saving, and the flow of capital to the developing world has increased, though with uneven results.
- *Macroeconomic adjustment* – inflationary conditions discourage investment, weaken the ability of relative prices to act as a guide to resource allocation, and act as serious discouragement to the private sector. Recently, inflation rates have come down almost everywhere in the developing world, and many countries have made significant progress in balancing their budgets (United Nations, 2000).

Achieving these reforms has not been easy, and there is now a vast literature analyzing the obstacles societies face in adopting policies that encourage openness. Much less attention has been paid, however, to the fact that even as openness is achieved, many developing countries are still failing to generate strong economic growth. There is, of course, no single explanation for these failures. The international economy is fast moving and demanding. Thus it is not sufficient for countries to simply dismantle inefficient industries in order to reallocate resources to traditional exports, themselves often of declining value. Countries must engage in a continual search for new competitive advantage, and strive to develop capacity in high-productivity sectors. Coherent price signals are therefore needed to steer resources toward promising new export sectors. Exchange rate policies are extremely important in this respect. Often, trade liberalization is accompanied by capital inflows that appreciate the exchange rate. This ends up stimulating the production of non-tradables rather than encouraging nascent exports.

The experience of the successful Asian countries is instructive. For over two decades, while their exports grew at unprecedented rates, the Republic of Korea and Taiwan (Province of China) were able to stabilize their real exchange rates through active management of the market. This clearly contributed to their export performance. On the other hand, experience shows that countries using the exchange rate as an anchor for domestic prices have found that real exchange rate appreciation is very difficult to avoid, with adverse effects on the growth of new exports.

However, even when price signals are strong, supply responses to price signals are weak in many developing countries. Markets are often segmented regionally and labour may be geographically immobile as well as uninformed about risks and opportunities. Small producers are unable to seize new opportunities due to poor levels of education or health, a lack of organizational or technological capabilities, or inadequate access to financial markets. Poor quality management, meanwhile, can leave larger enterprises unable to respond rapidly to changing market conditions. Meanwhile, with FDI, investors look for resources relevant to their needs before committing themselves to investing in a particular country. With the emergence of increasing numbers of high-value industries, human assets have become a crucial factor for investment decisions. Thus the capacity, flexibility, and initiative of a country's human resources have come to lie at the heart of many, if not most, investment decisions.

Finally, increased capital flows can pose serious threats to the stability of a country’s economy. While direct investors are likely to have at least a medium-term stake in a country’s future, portfolio investors and foreign creditors have tended to exhibit herd-like behavior. Waves of enthusiasm in “emerging markets” have given way to waves of panic (Radelet and Sachs, 1998; Furman and Stiglitz, 1998). The result has been extraordinary booms, followed by deep recessions. These have had demonstrable effects on human and social development. The East Asian financial crisis has not only had economic effects, such as bankruptcies, increased poverty, and rising unemployment, it has also led to reduced schooling, diminished public services, and increased social stress and fragmentation. While the Asian economies are now recovering, the adverse social effects are proving long-lasting (UNDP, 1999). Meanwhile, there is little evidence that countries have increased their ability to manage foreign capital flows, or have reached consensus on the features of "a new international financial architecture" (see Eichengreen, 1999; Ocampo, 1999, Agosin and Ocampo, 2000; Aluhwalia, 2000).

In sum, the liberalization of markets is a necessary condition for rapid, SHD centred growth. But is highly insufficient, for two reasons. First, it must be adequately managed, at the national and international levels. Second, countries must ensure strong supply responses to new price signals from a wide variety of actors, including foremost the poor. We deal with this latter issue when we discuss Sphere 3.

Sphere 2: The promotion of fast economic growth

Liberalization offers great economic development opportunities to a country, but active policies are needed to ensure those opportunities are taken up. Coherence in policymaking is also needed if fast and sustained economic growth are to be promoted. By establishing growth-friendly policies, policymakers not only increase international confidence in the development prospects of their countries, they also enhance domestic confidence that the future can offer rising levels of prosperity.

Economic growth depends upon factor accumulation and improvements in total factor productivity (TFP). In recent years our understanding of factor accumulation has been broadened by a wider appreciation of the nature of capital. Physical capital has become less important, as knowledge or information-based products and services grow in value. Even in traditional industries, a growing information element may come to constitute the core of competitive advantage and be the source of most profit (Evans and Wurster, 1999). The “knowledge economy” is thus increasingly reliant on the accumulation of social and human capital (and this will be discussed in more detail in the next section).

The accumulation of physical capital depends on the rate of investment in an economy. While FDI and other international capital flows can make a contribution to financing investment, domestic rates of saving remain crucial. In East Asia, for example, saving rates have been exceptionally high (averaging over 30 per cent for decades), enabling these countries to achieve the level of investment necessary to sustain rapid growth. In other regions, however – Latin America is a good example – saving rates have been much lower. In most developing countries, including those introducing economic reforms, investment rates have rarely surpassed 20 per cent of GDP. This is well below the 25-30 per cent that is needed to raise growth of income per capita to more than 5 per cent per annum over the long term.

Many factors act to depress domestic saving. Excessive government involvement in financial markets and inflation both discourage saving, and so does lack of public confidence in the soundness of domestic financial systems. Rather than providing a sound prudential regulatory framework, in many countries governments engage in unjustified intrusions into financial markets that distort the allocation of financial resources.

It is not enough for markets to attract savers. They must also be able to deliver capital to those in need of credit. Micro enterprises and small firms are typically cut off from financial markets. For those who do have access, in many developing countries, the spread between the rates of interest paid to borrowers and those demanded from lenders is notably high, reflecting lack of competition, inefficiency and the high-risk nature of their financial markets.

Policy makers therefore need to facilitate a well-functioning financial sector by offering a stable and predictable macroeconomic environment as well as a regulatory environment that upholds the rule of law, respects private property, and promotes the enforcement of legitimate contracts. Prudential oversight of the banking system to ensure, for example, adequate bank capital, reserves for bad and risky loans, and restrictions on loans to related parties are also necessary to inspire confidence in the system. Without such confidence, financial markets will be less active and savings will be concentrated offshore.

Private and public investment are often complementary. For example, without roads (typically built by governments), private investment for large markets is just not feasible. There are a large number of constraints to efficient public investment. Budget cuts in the context of macroeconomic adjustment policies have tended to fall disproportionately on public investment. In other cases, governments have attempted to do too much at the same time, overestimating their capabilities to carry out investment projects efficiently.

Sphere 3: Sustainable Human Development

The case for giving increased priority to sustainable human development (SHD) has been advanced on many fronts over recent years. Two main arguments have been made:

- SHD is the ultimate end of the development process, with economic growth simply representing an important means to that end. This view has been strongly advanced by the United Nations Development Programme (UNDP), which opened its first *Human Development Report* with the following statement:

  > The real wealth of a nation is its people. And the purpose of development is to create an enabling environment for people to enjoy long, healthy and creative lives. This simple but powerful truth is often forgotten in the pursuit of material and financial wealth (UNDP, 1990).

- There is growing evidence that, as well as being the main objective of broad-based development, SHD is also an exceedingly powerful *instrument* of economic growth and development. Human and social capital are increasingly recognized as an economic input, not simply an output, and there is powerful evidence that these forms of capital are becoming more important for economic development.

In discussing human and social capital, we note the importance of both as legitimate ends to development, but also explore their role as a vital instrument in the development process itself.

Human capital

The study of human capital focuses on the role of people in society, with increases in human capital improving the opportunities that people enjoy.[4] Education, for example, increases social mobility, allows enhanced participation in a range of social activities, and has well-documented effects on health and perceptions of quality of life. It is also an

---

[4] This is the perspective taken by Amartya Sen (1999), Nobel Prize winner in Economics for 1998. Sen prefers the expression "human capabilities" to the more conventional one of *human capital*. We retain the term "human capital" but give it the scope of Sen's "human capabilities".

important determinant of economic growth, offering clear private and public economic benefits. The better educated are more productive and have greater opportunities to succeed in the labour market. With the knowledge economy demanding ever-greater levels of skills from its workers, educated people are in turn better equipped to respond to changing market signals. This is especially important when an economy must restructure. Asian countries with a strong developmental record during the latter half of the twentieth century have all placed a strong emphasis on improving both the quantity and the quality of their educational systems.

If education offers people *opportunity*, then health provides them with *security* – and its importance is increasingly being recognized (Bloom and Canning, 2000). The burden of poor health falls most squarely on the poor in any society. Not only do they have the worst access to quality healthcare, but they also rely most on their labour – and poor health reduces people's ability to work. A health shock can quickly wipe out the savings of a poor or middle-income family in a developing country, while simultaneously decreasing investment in other forms of human capital (as a child is removed from school, for instance, both to save money and to act as a carer). Again, better health has measurable effects on the economy. Healthy people are better able to work, as well as more likely to save for their retirement and to invest in their (healthier) children's education. Improvements in health can significantly enhance the opportunities of the poorest in society.[5]

A related factor is demographic change, which offers all developing countries favourable economic opportunities in the years to come. Demographic change can be seen as a link between certain key aspects of SHD (better health and education, poverty reduction, gender equality) and faster economic growth. Demographic change is already happening everywhere, but poverty, lack of education, and inadequate access to health care can retard it significantly. *Per contra*, poverty reduction, improved education and health can act to speed up demographic change and can assist countries to reap a growth-enhancing *demographic dividend*.

As life expectancy increases, there is a lag before people start to choose to have fewer children. However, once fertility declines, it does so steeply (though how steeply varies from country to country) as people choose to invest more resources in fewer

[5] See chapter 6 of this book.

children. This demographic transition is at the heart of the development process. When large families are common, universal education is difficult to provide. Further, rural families look to their children to become productive on the land from a young age. The role of women also changes rapidly when smaller families are common. They are more likely to receive education and to become more active outside the family. This in turn increases the opportunities available to children, who tend to receive better education and more access to resources as their mothers become more highly educated.

Research shows that these processes can be accelerated by policies that actively promote the capability and autonomy of women and that seek to protect them from discrimination and physical abuse. Thus there is a clear positive relationship between the protection of gender equality, other elements of SHD, and economic growth.

Demographic transitions clearly have economic effects. Reductions in mortality initially affect infants and children most and set forces in motion that create a bulge (or "baby boom") in the age distribution. More specifically, the mortality decline creates the leading edge of the bulge while the trailing edge is formed by the subsequent decline in fertility. Once this enlarged cohort has been educated, they become available to the labour market, causing a sharp rise in the ratio of workers to dependents. If these workers can be gainfully employed, then a country has an opportunity to seize a substantial one-off *demographic dividend*. This demographic dividend is intensified by the high likelihood that the baby boom generation – with higher life expectancy and fewer children – will save more if the right policies are in place. (Bloom, Canning, and Malaney, 2000; Bloom and Williamson, 1998; and Bloom and Sachs, 1998). It may also be more entrepreneurial in its attitudes, as a consequent shift from country to town and city promotes more individualistic attitudes.

Social capital

The idea of social capital broadens human capital's focus on individuals to explore the importance of their relationships with others. The Human Development Index, according to UNDP, reflects "the most basic human capabilities – leading a long life, being knowledgeable and enjoying a decent standard of living". These are measured through life expectancy at birth, educational attainment (adult literacy rate and combined primary and secondary enrollment ratio), and income per capita. However (as UNDP underlines), other choices are important to people, including political freedom and participation, the development of the family, the rights of women, and social cohesion (especially, the avoidance of crime and corruption).

Democratic government balances the rights and responsibilities of citizens – and seems to be the form of government best adapted to the modern world.[6] The strength and effectiveness of a democracy – and popular confidence in, and support for, its survival – has important implications for the quality of life people enjoy. Democracies also seem most suitable to fostering values relevant to successful modern economies. The myth that pro-market reform can only be implemented under dictatorships has now been dispelled. Democratic governments have demonstrated that they are capable of designing and implementing far-reaching economic reforms, and that their politicians can build popular support for such reforms. In fact, without democracy, economic reform lacks legitimacy and can be easily turned back. It is also easier to foster widespread entrepreneurial attitudes within a democracy, as individuals enjoy the risks and benefits of taking responsibility for their own actions.

Strong democracies rely on institutional strength – which is also vital to economic development and the efficient functioning of markets, as the disastrous experience of the former USSR shows. Russian democratization and market liberalization were accompanied by rapid deterioration in almost all institutions and, as a result, the country faces economic decay, increasing poverty, and a precipitous decline in health status (Becker and Bloom, 1998). Even countries with functioning institutions cannot afford complacency, as a rapidly evolving environment (owing, among other things, to integration into the global economy) requires appropriate institutional responses. Many institutions find this process of continual reform difficult to achieve. Rich and poor countries alike are struggling with a reliance on outmoded institutions that continue to offer poor value and levels of service.

Social capital describes more than the formal relations in society, however. Indeed, many have argued that it is best confined to describing informal relations. For example,

[6] The number of democracies increased rapidly in the last decades of the Twentieth Century. For a more detailed discussion, see Dahl (1998).

Fukuyama (1999) argues that “social capital can be defined simply as a set of informal values or norms shared among members of a group that permits cooperation among them”, but warns that the sharing of values and norms does not automatically produce social capital. Some cohesive groups, for example organized criminal gangs, may substantially diminish a society’s share of social capital. Unlike human development, social development is thus much harder to analyze and measure. It is also much more difficult to say which social *change* is likely to contribute to significant levels of social *development*.

Social capital may be interpreted as the degree to which society promotes the identification of individuals with its institutions. In a society with a great deal of social capital, individuals restrict the range of their actions to those that promote the growth of the economy and the strengthening of its institutions. This requires building social institutions that reward individual effort in a fairly equitable manner. In other words, a minimum degree of *equality of opportunity* needs to be present. Thus it can be said that, in its broadest sense, the accumulation of social capital lessens conflicts of interest and channels the efforts of individuals towards goals in which individual enhancement is aligned with the common good. This positive outcome requires that individuals perceive that they have a stake in their society and will, therefore, want to work to promote its development.

Tools for building social capital relate to policies that foster equality of opportunity. In this area, the availability of quality education and healthcare is essential. As already noted, participatory democracy in which individuals feel that they do make a difference in the way their society is run is another important tool.

III. Interactions

None of the three policy spheres can be developed in isolation. Fast economic growth is exceedingly difficult to achieve in isolation from global markets. Technology now advances too rapidly for any country to proceed alone, and knowledge shows little respect for national borders. Policies to encourage openness, however, are impossible to sustain without economic growth. Global markets change fast and demand economies that are responsive to their signals. Sluggish economies will not experience sufficient benefits from liberalization to offset the inevitable costs. The consequences for all societies, and especially for democracies, will be growing protectionist pressures and reversals of liberal policies.

Nor can economic development be seen in isolation. SHD is the ultimate aim of development policy, but it is also a vital route to economic development and to enabling a society to benefit from openness. However, SHD cannot be pursued by itself and is illusory in the absence of economic growth. While it is possible for a society to get richer without its poorest people seeing their prospects improve, it is unheard of for large numbers of people to escape poverty while the economy as a whole remains stagnant or suffers reverses. Equally, an open society offers many advantages to those trying to achieve human development. Enhanced communication and a greater awareness of living conditions in other societies is a fundamental threat to repressive regimes – and liberal policies stress individual responsibility, which is impossible to achieve when human and social capital have been diminished.

By working at the intersection between the policy spheres – and creating a balanced policy portfolio – policymakers can seek to set up a positive feedback loop between different policy elements. By delivering sustained improvements in health, for example, policymakers will create a direct effect on demography, investment in education, physical capital accumulation, and the efficient functioning of the labour market. Further, smaller families spend more on the health of their children. And just as the educated are better able to extract benefits from health systems, as well as be more receptive to preventive health messages, so do those with productive jobs spend more on nutrition and healthcare.

Similar interactions can be seen across all policies. Formal analysis, for example, has been used to explore the interaction between demography and openness to trade. A country whose working age population grows at 3 per cent a year (and twice the pace of overall population growth), can reap a demographic dividend three times as large if its economy is open. In other words, a rate of growth of the working age population of 3 per cent boosts output growth by 1.5 per cent in open economies, as compared to only 0.5 per cent in economies that are not open to world trade (Bloom *et al*., 2000). Policy makers should, therefore, strive to achieve *virtuous spirals* whereby the outputs of interactions between policy elements generate a positive and reinforcing set of development benefits.

Conversely, policymakers must also act quickly and decisively to tackle a serious deterioration in any policy area, as this risks starting a *vicious spiral* causing declines across other indicators. In Sub-Saharan Africa, for example, the AIDS epidemic is having a dramatic effect on life expectancy, the productivity of the workforce, and the ability of parents to invest in their children's future. As a result, the wider prospects of the region are deteriorating rapidly.

The differences between the conventional approach to development and our advocacy of working at the intersection of policy spheres can best be visualized with the assistance of figures 2.2 and 2.3. Figure 2.2 is a flow chart outlining in a drastically simplified manner the stylized facts of the conventional approach to development policy. Briefly, this approach emphasizes, in one way or another, a trickle-down model of human development. SHD is viewed as the end result of policies that first promote growth. For example, as in the flow chart shown in figure 2.2, the accumulation of capital and productivity improvements lead to higher growth, which raises wages and increases tax revenues. These in turn induce an increase in both public and private expenditures in health and education, both of which lead to an improvement in wellbeing (SHD, in our scheme).

[Insert figure 2.2]

The view of development *from* SHD is quite different, and it is illustrated in the flow chart shown in figure 2.3. For illustrative purposes, we concentrate here only on efforts to raise public expenditures on health and education, but we could have taken any other point of departure (for example, efforts to promote greater gender equality). Improvements in peoples' access to good health and education have a number of positive effects on SHD directly and on an economy's capacity to grow. Better health and education by themselves broaden people's choices: they live better and longer lives, and these, in their own right, must be counted as important steps toward development. In addition, they have positive effects on growth. In the first place, women who expect to live longer and are better educated prefer smaller number of children with a higher quality of life. Therefore, fertility rates decline, and families spend more of their own incomes on the health and education of their children. The enhanced private and public expenditures on health and education have positive effects on productivity and competitiveness. On the other hand, as people live longer lives, they increase their saving for retirement, which also has a favourable impact on long-term growth processes.

[Insert figure 2.3]

The value of these simple examples is to illustrate the powerful outcomes that can be obtained from working at the intersection of policy spheres. Of course, as already noted, the positive effects of enhancing directly SHD-related variables will be greater in an open economy than in a closed one. In an open economy, people have the entire world as potential suppliers of their needs and as potential users of their products. But they must be given the proper tools to respond productively to the stimuli they receive from the broader world into which they are integrating. They must also be protected against the traumas that are likely to arise during the transition to a more internationally integrated economy.

IV. Action points

It may be claimed that our emphasis on three highly complex and multifaceted development policy spheres makes the task of governments all but impossible. Can governments act at once in a large number of directions? One of the basic problems of developing countries is the poor capacities of governments to deal with the multifaceted problems posed by development. This is certainly one aspect of the much-abused call for better governance in developing countries.

The concept of the virtuous spiral provides a route out of this impasse, offering the opportunity to take complexity into account, act in a limited number of directions, and adopt a number of different approaches. Instead of advancing on all fronts, governments can identify strategic points of entry that can be used to push the spiral into action. If governments succeed in identifying the strategic points of entry, they can set in motion virtuous spirals, with effects on variables in other policy spheres. However, as the first benefits are released, it is important to ensure that governments shift their attention to other areas of the policy portfolio. Balance, in other words, is most practically achieved as a *dynamic* process, rather in the way that a cyclist stays upright by continually adjusting to a permanent state of disequilibrium.

One consequence of this approach is to sound a long overdue death knell for the single model of development. Whatever the idea may be, it usually claims dogmatically to be the only fruitful approach to the development problem. Of course, the "right model" changes with the intellectual fashion *du jour*. Instead, it is increasingly recognized that there are now multiple models that can deliver results (though there are many more models that are unlikely to be successful). There is also some evidence that a bias towards human development is more likely to start the spiral moving than a bias towards short-term economic growth. Ramírez, Ranis, and Stewart (1997) argue that countries displaying “human development lopsidedness” moved to virtuous spirals in around a third of the cases, while all cases of “economic growth lopsidedness” resulted in only temporary gains. They also suggest that models need to change as progress is made, with basic health and education favored in the earliest phases, but resources gradually being shifted towards science, technology, and more advanced education. They also note that labour-intensive rural employment may be an initial priority, but economic growth in higher-productivity sectors will be essential to sustain growth.

Another consequence is to emphasize the need for co-operative actions between developed and developing countries. It is now amply clear that development will not occur unless developing countries pursue a portfolio of policies that leads to SHD *and* growth at the same time. It is also clear that the international environment must be helpful to the efforts of developing countries to promote their own development. Otherwise, such efforts will fall on barren soil.

Currently, it is possible to identify a number of strategic points of entry that offer policymakers an opportunity to make significant development progress. Examples include:

☛ *Tackling social exclusion*. To date governments have been less than successful in shielding the most vulnerable groups in society from the disruption of pro-market reform. Reforms are therefore threatened by rising inequality. Measures to tackle social exclusion have two aims. The first is to increase the security of the socially excluded through safety nets protecting the vulnerable members of society from the inevitable social side effects of a liberalized market economy.[7] These safety nets should be structured in

[7] For a similar view, see Rodrik (1997).

ways such as to induce individuals and groups to move towards increasingly independent and risk-taking behavior, rather than simply encouraging dependency (as, for example, have many developed country welfare systems). The second aim is to enhance opportunities by offering the excluded a range of ways to increase their participation in society, through education, support for small businesses, micro-credit facilities, and so forth.

☛ *Poverty reduction*. Inequality is a significant drag on society, especially in countries where a significant minority, or a majority, of people lives in poverty. Poverty is associated with higher fertility, which impedes the demographic transition. It also diminishes the demand for education. Large numbers of poor people also make a country more vulnerable to disasters and to internal wars. Sri Lanka, for example, is frequently praised for the priority it has given to human development. Poverty levels, however, remain high, a civil war has cost tens of thousands of lives, and few would claim that the country has made broad development gains in recent years. Pro-poor growth should focus on achieving and ensuring the maintenance of full employment; removing anti-poor biases from macroeconomic policies[8]; investing in the capabilities of poor people; ensuring the access of poor people to resources, including credit; increasing the productivity of small-scale agriculture and small businesses; and promoting labour-intensive industrialization. These approaches to development policy are very much in line with UNDP's emphasis on SHD.

☛ *Support for small business*. The small business sector is increasingly important to modern economies, but many small businesses – especially in developing countries – suffer from low productivity, lack of skills, and archaic methods of production. In fact, many such “businesses” are no more than a symptom of disguised unemployment. Action to strengthen the small business sector can help mitigate unemployment by transforming underemployed workers into self-employed entrepreneurs, who may

[8] It is a well-known fact that macroeconomic adjustment programmes often include cuts in expenditures that benefit the poor.

eventually employ others, while improving skills, increasing access to technology, and providing access to credit for working capital and investment.

Recent experience shows that a particularly useful point of entry is support for financial institutions catering to the needs of micro and other small enterprises. There are a large number of successful experiences in the developing world with financial institutions that rely on innovative credit technologies for delivering services to micro enterprises and small firms. The most famous example is, of course, the Grameen Bank in Bangladesh. But there are many others, including Banco Sol in Bolivia, Fundación Calpiá in El Salvador, Bank Rakyat Indonesia *unit desa*, etc. (Morduch, 1999; also, see chapter 7 of this book). These innovative institutions allow poor people and small firms to help themselves by enabling them to become entrepreneurs. Policies to promote these institutions are an example of working at the intersection of policy spheres: they are welfare-enhancing in their own right and thus promote SHD, and they also foster growth by enabling people to raise output and investment. Such efforts need the support of the international community.

Action targeted at potential entrepreneurs is effective even when people move into other forms of employment, helping to create employees with the "intrapreneurial" attitude that modern businesses value. Most exciting, today's first generation entrepreneurs may breed a second generation with vastly increased ambition and scope.

☞ *Higher education*. Today higher education has become, in many ways, the basic education of the knowledge economy. Yet in developing countries resources for higher education, and indeed higher education systems themselves, remain very inadequate. Urgent action is therefore needed to plan their expansion and diversification as well as to build systems that will meet the requirements of tomorrow's world. Enhanced higher education will not only lead to better trained graduates, it will also provide developing countries with important points of contact with the global economic 'commons' as well as exerting upward pressure on education *quality* throughout the rest of the education system.

☞ *Action on health*. As argued above, improved health is crucial to combating poverty, while health shocks can threaten the whole development process. As successful immunization programs have shown, action on health is especially suitable for international co-operation. There are many areas where renewed action is needed. In Eastern Europe, for example, deteriorating health (along with the breakdown of governance) is at the heart of the disastrous performance of many countries (see Becker and Bloom, 1998). HIV/AIDS, meanwhile, can be tackled through education and the effective marketing of health messages (as the examples of Uganda and Thailand show). A renewed global campaign, with substantial private sector involvement, could have a huge impact on the prospects of much of the developing world.

An especially contentious area, needing international discussion and action, is access to pharmaceuticals. Once a drug is developed, the cost of producing it is low, and there is surely scope to exploit the difference between the market price and marginal costs to ensure that people the world over can have access to drugs that can make them happier and more productive. Imaginative solutions to this problem could form the basis for a future international agreement on health. A start in the field of AIDS has already been made with the willingness of pharmaceutical companies that have developed drugs for this disease to market them in developing countries at an eighth of their price in developed countries. We recommend that a new *Compact for Global Health* be launched under the auspices of the World Health Organization, with the support of national governments and private firms. The Compact would have as its major objective to generalize the practice of providing pharmaceuticals to people in developing countries at marginal cost. It would also seek to ensure that this practice becomes feasible through policies that prevent unlawful arbitrage between markets.

☛ *Institutional renewal*. The need for new forms of governance has already been discussed. In a global economy, there is also a need for strong international institutions as well as for action to equip national institutions to engage more effectively within the global system. The disastrous recent WTO negotiations in Seattle demonstrated how much work there is to be done. The negotiations revealed widespread public disillusion with globalization, showing how poorly policymakers have articulated the case for openness. They also revealed damaging splits between developed and developing countries. Developing countries have been told that liberalization is the best policy, but they have not always found markets in developed countries opening for them. Many developing countries have also been shown to lack the capacity to negotiate effective agreements. Technical and financial assistance is also clearly needed to help countries implement new trade rules and to adapt to new requirements in the North. While they may be intended to improve consumer protection, they are all too often criticized from the South's perspective as examples of, in effect, covert protectionism.

There are needs for greater governance at the international level in other realms as well. International finance has the first priority on the list. The most recent world financial crisis revealed that the globalization of finance has proceeded at a much faster speed than the capacity of the international system to govern international finance so as to ensure that it contributes to development. The crisis and its aftermath showed that financial crises can inflict enormous harm on fragile countries and that there exists an urgent need to work in the design of an international financial system that serves the needs of people everywhere.

Poised on the threshold of a new century, policymakers across the world have a great opportunity – and responsibility – to help define this new epoch. The last century delivered a number of major improvements to the lives of many of the world's poor, disadvantaged, and excluded. Yet there is still much work to be done. New technology has profound implications. It can help disseminate decades of developmental 'knowledge capital', and open up an incredible range of new opportunities. Equally profound, however, is the responsibility on all of us to help ensure those opportunities are used to deliver a humane, liberal, and global future for all of our planet's inhabitants.

REFERENCES

Agosin, M. R. (1999), "Liberalization and the International Allocation of Foreign Direct Investment", Working Paper No. 8, Center on International Economics and Development, Universidad de Chile, Santiago.

Agosin M. R. and J. A. Ocampo (2000), "La Arquitectura Financiera Internacional: Hacia la Creación de un Marco Propicio para la Estabilidad de los Mercados Financieros y Cambiarios", CEPAL, November, unpublished.

Ahluwalia, M. S. (2000), *Reforming the Global Financial Architecture*, Commonwealth Secretariat, London, April.

Becker, C. and D. E. Bloom (1998), eds., *The Demographic Crisis in the Former Soviet Union,* Special Issue of *World Development*, November.

Bloom, D. E., and D. Canning (2000), "The Health and Wealth of Nations", *Science*, February.

Bloom, D. E., D. Canning, and P. Malaney (2000), "Demographic Change and Economic Growth in Asia," *Population and Development Review*, forthcoming.

Bloom, D. E., D. Canning, D. Evans, B. Graham, P. Lynch, and E. Murphy (Bloom *et al*., 2000), "Population Change and Human Development in Latin America," background paper prepared for Inter-American Development Bank, *Economic and Social Progress in Latin America, 1999-2000 Report.*

Bloom D. E., and J. G. Williamson (1998), "Demographic Transitions and Economic Miracles in Emerging Asia," *World Bank Economic Review*, **12**: 419-55

Bloom, D. E., and J. D. Sachs (1998), "Geography, Demography, and Economic Growth in Africa," *Brookings Papers on Economic Activity*, **2**: 207-295.

Dahl, R. A. (1998), *On Democracy*, Yale University Press, New Haven.

Eichengreen, B. (1999), *Toward a New Financial Architecture – A Practical Post-Asia Agenda*, Institute for International Economics, Washington, DC.

Evans, P., and T. S. Wurster (1999), "Getting Real About Virtual Commerce*", Harvard Business Review*, November-December.

Fukuyama, FF. (1999), *The Great Disruption: Human Nature and the Reconstitution of Social Order*, The Free Press, New York.

Furman, J. y J. E. Stiglitz (1998), "Economic Crises: Evidence and Insights from East Asia", *Brookings Papers on Economic Activity*, **2**: 1-135.

Morduch, J. (1999), "The Microfinance Promise", *Journal of Economic Literature*, **37**: 1569-1614.

Ocampo, J. A. (1999), *La Reforma del Sistema Financiero Internacional: Un Debate en Marcha*, Fondo de Cultura Económica, Mexico City and Santiago.

Radelet, S. and J. D. Sachs (1998), "The East Asian Financial Crisis: Diagnosis, Remedies, Prospects", *Brookings Papers on Economic Activity*, 1998, **1**: 1-90.

Ramirez, A., G. Ranis, and F. Stewart (1997), "Economic Growth and Human Development", Yale University Economic Growth Center Discussion Paper No. 787, December.

Rodrik, D. (1997), *Has Globalization Gone too Far?,* Institute for International Economics, Washington, D.C.

Sen, A. K. (1999), *Development as Freedom*, Knopf, New York.

United Nations (2000), *World Economic and Social Survey 2000*, New York.

United Nations Conference on Trade and Development (UNCTAD, 2000), *World Investment Report, 2000*, Geneva and New York.

United Nations Development Programme (UNDP, 1990), *Human Development Report, 1990*, New York.

UNDP (1999), *Human Development Report*, *1999*, New York.

World Bank (1999), *World Development Indicators, 1999*, Washington, D.C.

Figure 2.1

The three spheres of development policy

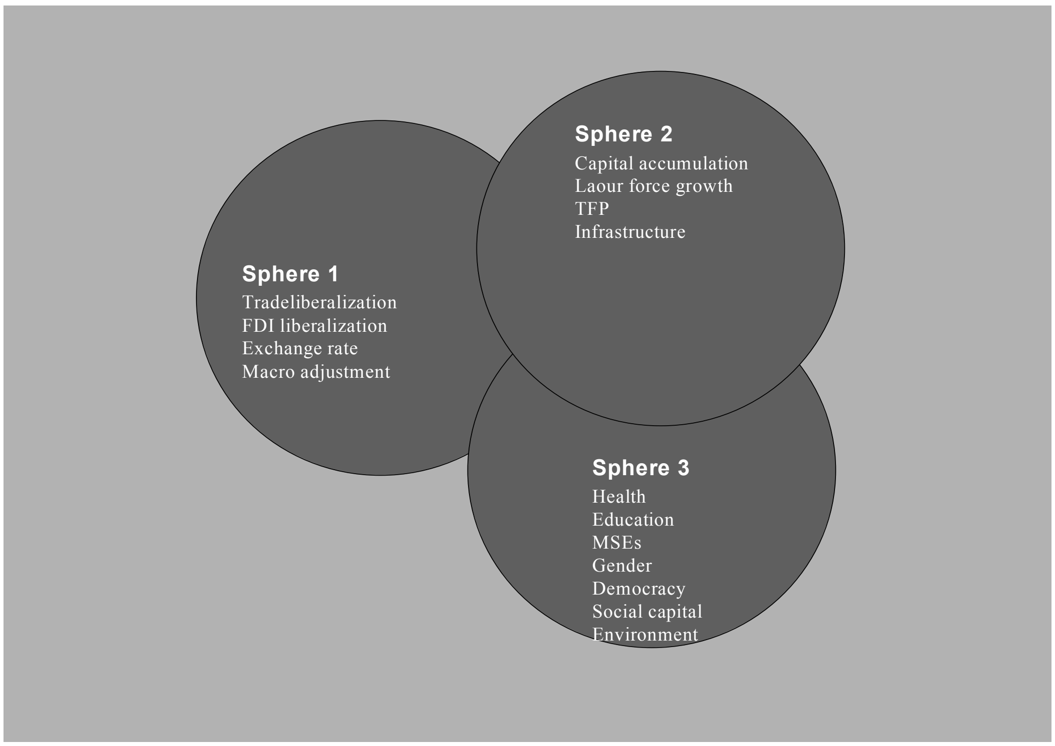

Figure 2.2

The conventional approach

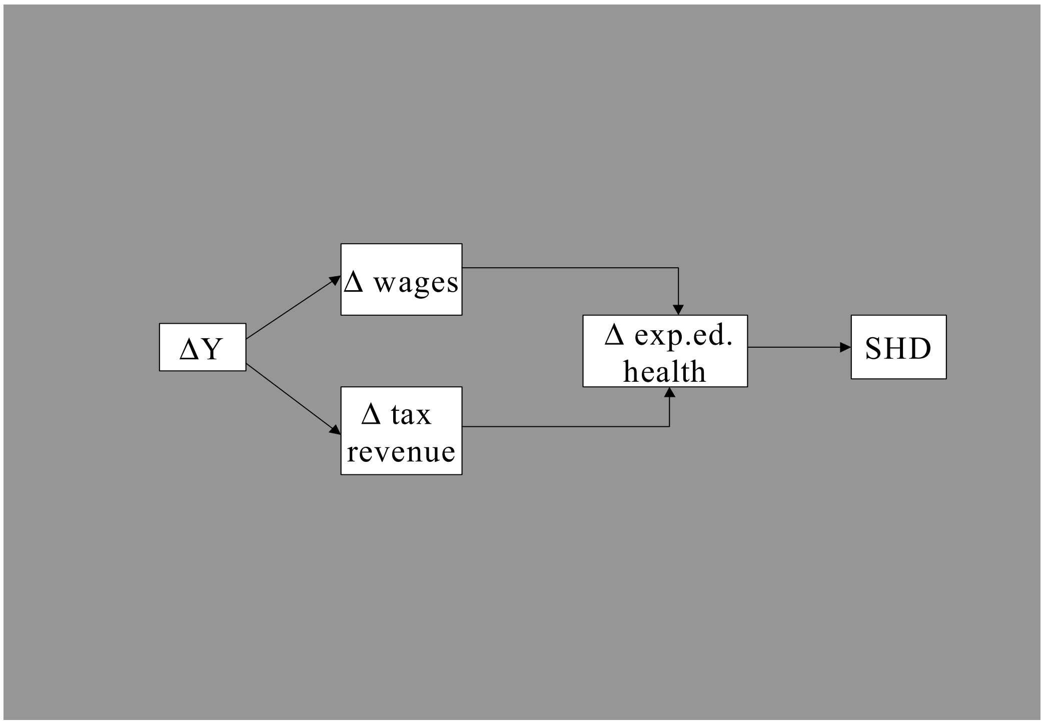

Figure 2.3

The vision *from* SHD