Institute of Social Studies

Balanced Development

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Preface

This paper has been prepared as an inaugural address to be presented at The Institute of Social Studies in The Hague on 30 March 1995.

In preparing the paper I have been conscious of my debt to various colleagues and collaborators, several of whom are mentioned by name in the text. Here I would like to acknowledge Hans von Sponeck who stimulated my work in Pakistan both in his capacity as the former UNDP Resident Representative in Islamabad and, emerging from that, as a friend. I would also like to express here my debt to my wife, Shirley, for all her support.

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Introduction

While economists and others might disagree over the most appropriate policies for stimulating development, there is at least some convergence of views on objectives. The appropriate means may be in doubt, but the end that is commonly understood is to raise living standards on a sustainable basis.

Regrettably, this agreed objective has become more difficult to achieve in the aftermath of the debt crisis in the early 1980s. While there were several important aspects to this crisis, two points in particular can usefully be mentioned here. Firstly, the debt crisis marked the point in time at which the net transfer of resources from developed to developing countries started to decline. This transfer is now substantially negative for many would-be recipients. Secondly, and not unrelated to the first point, it was also at about this time that real interest rates increased sharply as a direct result of a shift in the macroeconomic policies adopted in the developed world. This brought to an end an era in which debtor nations could rely on inflation to amortize their obligations to service debt.[1] There has, therefore, been a major structural change in the context within which the developing countries are now attempting to raise the living standards of their people. Under the new regime, debts are more difficult to pay off, which implies that the premium on export earnings and private direct investment as preferred sources of foreign exchange has increased. In other words, the balance-of-payments constraint on development has tightened for most countries.

It was in this relatively more hostile environment that, at some point during the 1980s, many countries were obliged to embark on structural adjustment and stabilization programmes as orchestrated by the Bretton Woods institutions. Growth ground to a halt, and became negative in a number of countries, not because of the programmes themselves but because of the external imbalance to which they responded. Living standards suffered accordingly, so that the 1980s have been referred to as a 'lost decade' in the quest to reduce poverty.[2] Indeed, the proportion of the world's people who are poor has probably risen, while the absolute number has almost certainly increased.[3] Moreover, the gap between the richest and poorest countries has grown rapidly and continues to do so. The world has become less equal over the past decade and the differences are increasing.[4] In this technical sense, if no other, the situation is explosive.

Since the poor of the world are the last among those who might be blamed for the balance-of-payments problems that their countries have encountered, it seems less than fair that they should have to share in the costs of re-establishing economic viability. An influential book, *Adjustment with a human face*, published in 1987 on behalf of UNICEF, signalled this injustice and, in doing so, made the point that the cost of maintaining the fragile safety nets which some poor countries could previously afford would be a small price to pay for the poor's protection.[5] By the same token, protection of the basic services enjoyed by the poor would be unlikely to jeopardize in any serious way the elimination of the fiscal deficits which had led governments to borrow in the first instance. Moreover, it is argued that the longer-term prospects for development, which depend crucially on the health and education of children, should not be sacrificed for the sake of short-term economic stability. Hence the Bretton Woods institutions in particular have been pressured to reaffirm the importance for development of the social dimension, and to strive for a more appropriate balance between economic and social concerns in the determination of policy. Perhaps the most visible expression of these concerns has been the annual publication, beginning in 1990, of a *Human Development Report* (HDR) by the United Nations Development Programme (UNDP) which serves as a point of reference for much of the current debate on appropriate strategies.[6] Less well known is a set of four country studies which were commissioned by UNDP to articulate at country level some of the concerns that were being expressed in the HDRs. I was responsible for one of these studies, the report on which has been published in summary form under the title *Balanced development: an approach to social action in Pakistan*.[7]

The work undertaken in Pakistan with various colleagues[8] served to reinforce my concern that many of the issues which are crucial for human development lie beyond the scope of standard economic analysis and the existing calculus of costs and benefits. There were then two options. One was to extend the range of that calculus by building on a number of basic economic concepts, notably the gross domestic product and human capital, so as to embrace a wider range of issues. I will refer to this option as the supply side approach. The other possibility was to accept the limitations of existing theory and to argue the cause of human development as being worthwhile in its own right. I will call this alternative the demand side approach.

In opting for the supply side, I was well aware that my choice was controversial. Equally, I think it was the right choice to make and, in the final section of this paper, I will elaborate on my reasons. For the present it may suffice to note that an important concern at the time was to invoke the *prima facie* case for donor support of social sector projects or reforms which could be shown to be attractive when costs and benefits were computed with reference to appropriate market or shadow prices.[9] Not least, the need for a shift of the aid budget from physical to human capital investment might be promoted more effectively within such a conceptual framework, with the alternative being to have to rely on the arguable merits of such a proposal in the specific context of Pakistan.

This need to strike the right balance between policies, projects and reforms which are often, and somewhat misleadingly, classified as being either 'economic' or 'social' explains why the title *Balanced Development* was chosen for the report on Pakistan. It was, therefore, a happy coincidence to discover subsequently that this same expression was being used in this same sense more than thirty years ago within the United Nations. In particular, the 1961 *Report on the World Social Situation* was subtitled as being 'with special reference to the problem of balanced social and economic development' and a special study of the subject was presented as Part II of that document.[10]

This coincidence and the intrinsic interest of the arguments presented might have been sufficient reasons for devoting a section of the present paper to the various findings of this 1961 UN study, following the introduction in the next section of some extensions of the economic calculus which respond to my concern that a supply side approach should be developed. However, the case for discussing the 1961 document becomes irresistible once it is appreciated that the study reported in Part II of that document sets out many of the arguments that are now being invoked as intellectual foundations of the HDRs.[11] Moreover, the proposed resolution of certain methodological or research issues which arise in an attempt to identify what a human development strategy might look like are much the same in the two cases. Accordingly, there are two related versions of the demand side approach to be considered, and an attempt is made in section 2 below to do justice to the point of view they represent.

In the final section of this paper, section 3, I will try to reconcile the demand and supply side approaches and to elaborate on the sense in which they are mutually supportive. From my personal perspective, I find no difficulty in this. But I cannot speak for those who champion the demand side. For them the extensions of economic theory which are to be discussed in the next section may well be regarded as an unwarranted intrusion into the domain of humanist concerns.

1. Towards an extended calculus of costs and benefits

There is a very large literature criticizing the use of national income statistics in various contexts, not least as a measure of development.[12] Much of this can be traced back to Hicks (1942) who suggested that the national income was a measure not only of production but also of welfare. In my opinion this is not helpful and I prefer to regard the national accounts as being first and foremost a framework for recording the gross domestic product, preferably in the form of a social accounting matrix (SAM), which identifies all the different institutions in society and sets out exhaustively all the transactions between them. Institutions in this context refer not only to individuals, who may be clustered into socio-economic groups, but also to the corporate sector, government itself and the various non-governmental organizations (NGOs) which, taken together with individuals, constitute the society as a whole. With this as the starting point, the main difficulty which then remains is to decide which transactions to include in the matrix and which, if any, to ignore.

Most of the criticism which remains, once any claim to measure welfare has been dismissed, focuses on the fact that the domestic product accounts, as we might now call them, are largely confined to a record of transactions that are intermediated with money. Hence the gross domestic product as we know it is essentially a measure of the size of the monetary economy which leaves out of account most of the activity which takes place in the non-monetized sector. It has been argued, strenuously on occasion and with some merit, that this omission introduces a gender bias into the accounts which various authors have attempted to correct in more or less *ad hoc* ways.[13]

The most important omissions from the national product accounts of most countries are the goods and services (other than food) which are privately produced for personal consumption by a combination of domestically-owned durables (other than housing) and the time which is spent privately in producing them by members of the family. This means that no value is put on leisure nor on the role of families in raising children, caring for the sick or feeding the work-force.

One way of responding to these limitations is to impute some value (related to opportunity cost) to some of the individual items which are not otherwise recorded in the domestic product accounts. Another approach, which is ultimately the only one which can be satisfactory, is to recognize all time and household assets as being valuable resources which have a shadow price or opportunity cost. The extension of the domestic product accounts which is then called for is a complete statement of time use and the employment of consumer durables irrespective of whether or not their product is marketed. What I am suggesting, then, is a matrix accounting for all monetary transactions as the starting point and for this to be expanded by covering non-monetized transactions also in a complete accounting for all uses of scarce resources, in which the resources themselves are valued consistently at their opportunity cost.[14]

This radical approach has many far-reaching implications, one of which is that it leads to a very different view of what value added might be and where it is created. The economy must now be seen as having two 'halves' which may be comparable in magnitude and these are linked, one with another.[15] One of the halves is the monetized economy where goods and services are bought and sold, and the other is the non-monetary economy where goods and services are freely exchanged between individuals, typically within the same household. The supply of labour to the market is one important feature of the interface between these two parts. Another is the purchase of goods and services for what the conventional accounts refer to as final consumption. Given these links, of which the two mentioned are perhaps the most important, it follows that it cannot be sufficient to analyse what goes on in the monetary economy in order to understand the supply of labour as conventionally defined or the level of living standards: it is necessary to look into the non-monetary economy also in order to understand, for example, how price reforms or new incentives might influence behaviour, or the way in which structural adjustment affects poverty.

To articulate these concerns and to give substance to this approach, the standard model of consumer behaviour must be developed in several respects, building on Becker (1965) for the analysis of time use and by regarding the household as being simultaneously a consuming and producing unit.[16] In this framework leisure is a legitimate use of time which has a value that is based on its opportunity cost. And the supply of labour to the market is an intermediate output of the household and, therefore, not final. Similarly, wages are no longer a contribution to value added, but leisure is.

The purchase of consumer durables is one way of introducing a dynamic element into this re-formulation of *homo oeconomicos*. Another, which is more interesting, is with reference to human capital.

The standard formulation of human capital, based mainly on Becker (1964), regards education and training as the relevant investments, with the subsequent improvement in actual and expected earnings being the measure of benefits. A more general approach is needed for our purposes and this can be developed as follows. The individual is, among other things, an embodiment of human capital created, in the first instance, by an investment in reproduction which may or may not be enhanced subsequently through education, training or learning-by-doing. It then follows that, in order to capture this construction, the notion of investment in human capital must be extended to include the resource costs of a live birth, not the least of which are the risks to the mother of having a child. The gross return to this investment can now be defined as the value of an individual's time, however used, and should not be restricted to that part of the day, if any, during which the services of human capital are rented out for wages. The net return to investment in human capital is then obtained by subtracting from the gross return the opportunity cost of maintaining human capital, in other words, the necessary cost of maintaining the current and future potential of human capital. To adopt an alternative vocabulary, maintenance costs can be interpreted as the costs of satisfying basic needs and include the necessary allocation of time for rest and sleep[17].

This reformulation of individual behaviour can be enriched by allowing the utility of individuals to be interdependent, which then provides a motivation for the non-requited transfers which dominate the transactional relationships within a family. The reformulation admits a rich variety of individual behaviour and has some far-reaching implications. Two examples may suffice to illustrate this point.

If the satisfaction of basic needs is to be interpreted as the maintenance of human capital, then the cost of meeting basic needs represents intermediate consumption, not final, and is not, therefore, a part of value added. Hence, all basic needs should be exempt from value added tax. More generally, the argument that a value added tax is attractive because it is neutral breaks down if the definition of value added to which the tax is applied is not the correct one. In the approach being presented here it is implicit that production is being (re)formulated as output that is generated *via* the services of physical and human capital, both of which must be maintained.[18] This symmetric treatment has much to commend it. In Pyatt (1992a) it is shown to imply that value added will be equal to profits as we know them *plus* a return to domestic durable goods *plus* the value of time that is not absorbed by sleep and other maintenance activity. In other words, value added is being re-defined as a measure of the surplus that is generated by economic activity. To the extent that the distribution of this surplus is heavily skewed towards the rich, with the poorest getting nothing, a progressive income tax emerges as being more neutral than a value added tax (VAT) since VAT as we know it is levied on what I am now suggesting is an inappropriate measure of the gross domestic product.

Further illustrations of the way in which the proposed reformulation suggests new policy perspectives can be developed in relation to maintenance and subsistence. One point which can be made immediately is that the case for giving priority to the satisfaction of basic needs now emerges as a candidate for being among the best options for use of available funds from a supply-side point of view.[19] This is because help to those families that cannot meet their basic needs is likely to have a high pay-off for all of the same reasons that have been invoked for raising wages on the basis of efficiency theory. Individuals who are too poor to maintain themselves properly will be better placed to earn more if better fed. A further implication of this reformulation has a direct bearing on population policy. A subsistence household can be defined as one which generates little or no surplus over and above that which is required to reproduce itself. Since the return to human capital investment is measured through the surplus generated, the absence of any such surplus implies a zero economic rate of return to investment in reproduction for subsistance households. I do not interpret this result as Malthus might have advised but rather as a useful starting point in making a case for supplying contraceptives to those who want them by investing in clinics, advisory and distribution services, etc..

Optimal maintenance, both of ourselves and any physical assets we may own, is one of the conditions for achieving production efficiency which follows from the proposed reformulation of individual behaviour and motivation. Such conditions can, in turn, be derived from the conditions under which a Pareto optimum might be achieved. It follows that the proposed reformulation is not inconsistent with the standard case for free trade, perfect competition, control of monopolies, etc. There is, therefore, no inherent conflict between what is being proposed here and the standard prescriptions of public finance. For example, the control of pollution through indirect taxation remains a part of the first best solution. And, because time is to be recognized as a resource, corresponding arguments will now extend to those externalities which constitute congestion: these too, should be taxed.[20]

The control of externalities, preferably through taxation, is one way in which the proposed reformulation suggests that balance between economic and social concerns might be achieved. More important, possibly, is the fact that the complementarity of human and physical capital in generating most types of output (but not leisure) will imply that investment in both is likely to be necessary for intertemporal efficiency. Strict complementarity is not implied here since the criterion for deciding on which investments to pursue should be the net present value of each particular use of funds, not the amount of funds which might otherwise be allocated to particular types of investment. And here it can be noted that environmental conservation and reclamation projects can be included in the portfolio mix according to the familiar calculus of costs and benefits. In this sense the balanced development approach is able to embrace each of land, labour and capital in a symmetric reformulation of production possibilities and efficiency. The conclusions this leads to, as indicated previously, are neither radical nor surprising. Rather, the main consequence of this reformulation is to provide a more general framework for analysis which generates support from the supply side for policies which previously depended on the strength of *ad hoc* arguments and common sense.

We can go further, since the comprehensive treatment of time use which is the essential element in the proposed reformulation implies that, at least conceptually, all activities which involve human agency can be included within the framework. In principle, therefore, those activities which are involved in the maintenance and improvement of existing institutions or the creation of new ones, the drafting of new legislation or the policing of what now exists, can all be understood as contributions to the creation and maintenance of the fabric of society. Indeed, the maintenance of good governance is likely to be one of the very best uses of scarce resources in any society, while the promotion of the NGO sector may be an important second best alternative, to be pursued in those cases where governments cannot be relied upon. Indeed, the development of the NGO sector has a strong claim to being part of the first-best solution. Thus Banuri *et al.* (1994) promote the need for just such social capital formation within the new paradigm of sustainable human development that UNDP has recently adopted as the organizing concept for many of its activities. They make a clear case for maintaining social capital as defined and investing in its restoration and extension, drawing on the analogy between social capital and all other types of assets. In this they were able to build on the case for improved governance in Pakistan which was a particular feature of the *Balanced Development Report* cited above. That report may have placed less reliance on NGOs as a vehicle for social development than Banuri *et al.* might have wished, but it was deeply engaged in the substance of local government reform and the need for new institutions to make effective contact with people who are otherwise marginalized in their settlements and villages.

The fabric of society (or social capital) and social accounting are closely linked. The institutions of society define the structure of a SAM in the first instance, while the effectiveness of these institutions, including the networks which connect them, are critical determinants of the flows which take place, not only in the monetized economy, but equally in the private world of non-monetary transactions. It is in this context that the relevance of the household as an efficient vehicle for the generation of individual opportunities and freedoms should be seen. Its ability to function will then depend *inter alia* on having access to public services, labour markets, etc. Accordingly, there are important complementarities between human, physical and social capital that a balanced development strategy will want to exploit.

From the perspective of public finance, the services rendered by social capital are public goods which do not, therefore, have a market value.

But in theory, at least, this does not preclude the possibility of identifying the optimal level at which public goods (or services) should be provided. Conceptually, therefore, the balanced development approach can be extended to include them. Which is not to deny that, in practice, decisions to invest in the creation of social capital may well have to be made on the basis of a more commonsense evaluation of the extent to which, for example, an involvement in local politics is a constructive use of time.

2. A view from the United Nations, *circa* 1960 and again in 1990

The point was made in the introduction to this paper that there is a striking continuity from the view of balanced development expressed in Part II of the 1961 *Report on the World Social Situation* to the annual series of HDRs, the publication of which began in 1990. I therefore propose, in this section of the paper, to set out, firstly, the general line of argument which is developed in the earlier UN study and then to supplement this with reference to the more recent analysis offered by the HDRs themselves and, more particularly, the contribution of Anand and Sen (1994a) to a series of Occasional Papers which support the annual HDRs.

The starting point for the (unknown) authors of the UN study is to emphasize the various ways in which economic and social development are interlinked. They begin with the proposition that the 'importance of economic development as a means to social ends' is well known and can be taken as being more or less self-evident. The complementary argument, that social development is important for economic growth, is then developed in stages, the first of which is to note how social factors can impede such growth in various ways. The potential obstacles are elaborated under three headings: (i) population growth; (ii) institutional factors, such as a caste system; and (iii) individual factors, which are defined to include motivations and attitudes, not least in relation to savings and entrepreneurship. Set against these potential obstacles are the many positive ways in which social development expenditures can support economic growth, with the primary example being investment in human capital (which was then, and still is, treated as consumption, not investment, in conventional national product accounts). Health and education are singled out for special mention in this connection and it is suggested that there is no adequate way of distinguishing the economic benefits of such expenditures as distinct from their social implications. The report indicates that it would be (extremely) difficult to define the size of the eventual economic returns from a sewage disposal scheme or the building of a hospital (United Nations 1961: 33) and that 'The possible contribution of [a] school to material production is beyond measurement at the present time but not beyond conception' (United Nations 1961: 35).

Today, some thirty years on, it may be realistic to express somewhat greater optimism over the prospects for measuring the economic benefits of a school. Indeed, it is precisely that possibility which has been invoked in the previous section of this paper in suggesting that a calculus of costs and benefits can be developed to cover a wide range of economic and social activity. But such optimism is ultimately not essential for the point of view I want to argue here. For that, it is sufficient that such a calculus of economic costs and benefits is 'not beyond conception' to quote the study, since it is the conceptual basis of a human development strategy which is my main concern. The possibilities that now exist for illustrating my case can only serve to strengthen it. And there are, of course, many of these in the fields of health, education and the environment.

But this is not the end of the story since the authors of the 1961 UN report were evidently worried about something other than the technical difficulties of cost-benefit analysis. Specifically, they were concerned that precise knowledge of the interactions and independencies between economic and social variables 'will not *fully* indicate what the pattern of development ought to be, because questions of value also come in – the value to be placed upon, say, education for its own sake' (United Nations 1961: 38; emphasis added).

Faced with this undeniably reasonable proposition, the question of what to do about it cannot be avoided. There seem to be several possibilities. One would be to proceed, nonetheless, to conceptualize the problem of computing economic costs and benefits. Back in 1961, this might not have appeared as an attractive option, since the necessary theoretical developments were only just beginning to emerge. It is a realistic option today, however, and will be referred to here as the *a priori* approach. A second approach, which is hinted at in the UN study, is to set targets: 'the concept of balanced development clearly means for most people who use the term, an appropriate relation between economic and social factors – giving to each field or sector of development the attention it deserves in the total complex. It thus implies in the first instance a value or goal, something to be sought (even if only dimly perceived)' (United Nations 1961: 37) This, then, is an argument for pursuing a target approach as discussed in Kaul and Menon (1993). A third approach is to set aside the economics of scarce resources and to explore the actual experience of countries, looking for patterns in the data in an attempt to identify from the data themselves what actually seems to work and what does not. We can refer to this third possibility as the empirical approach.

In opting for the empirical approach, the 1961 UN report provides an illuminating analysis of the relationship between gross domestic product and various social indicators such as infant mortality, life expectation, school enrolment, calorie intake, etc. With due respect to the limitations of these data, various outliers are identified. For example, exceptionally good school enrolment ratios, relative to the gross domestic product, are noted for Ireland, Japan, Sri Lanka, Taiwan and Thailand, with a correspondingly poor performance being recorded for Venezuela and Cuba. Similar results in relation to infant mortality show Greece, Japan and Taiwan as doing well, while Chile and the former Borneo join Venezuela and Cuba as poor performers.

Investigation of the correlations which exist between various indicators and of the outliers which can be identified by such analysis is supplemented in the UN report by an exploration, for many of the same countries, of public expenditure patterns for the social sectors, mainly with reference to health, education and housing. A limitation of the analysis here is a failure to explore the extent to which the outliers previously identified might be explained by levels of public and private expenditure. But this would have been a very difficult undertaking in practice, since a functional classification of public expenditures was not available for many of the countries concerned, while household survey information on private expenditures was similarly scarce or non-existent. The analysis has many points of interest, nonetheless, including the authors' conclusion that there was little evidence in their data of defence expenditure crowding out the social sectors.

These various analyses were undertaken in the 1961 UN study on the basis that:

> The standard of living of a population – or, better, the 'level of living' – must be regarded as a set of components (health, nutrition, education, housing, employment condi-

> tions, etc.) which cannot be reduced to a single index. Insofar as the level of living is measurable, it must be expressed, not as a single quantity, but as a pattern of non-convertible quantities. The fact that the level of living is not to be defined as per capita national income does not deny, however, the underlying importance of growth of national income for the improvement of welfare.
>
> It follows from the above that it is impossible to say on any systematic grounds what a country's level in health, education, or other social component should be, given its level of economic development; or, again, what percentage of its national income it should expend in these fields. If an economically under-developed country is only one-third literate and has only one third of its children in school, there is no standard which will demonstrate that, say, one-half of the people should be literate and one-half of the children in school. Obviously, everyone should be literate and all children should be in school. (United Nations 1961: 38).

No doubt we can all agree to that. But the issue which concerns policy today is not one of where we eventually want to be but of how to proceed from where we are. It is in recognition of this practical need to proceed on an incremental basis that the UN study makes its strongest plea for the comparative study of experience in different countries:

> If countries have a long historical experience in development and a familiarity with the interactions of economic and social factors, plus an educated population aware of its needs and articulate about its values, and a leadership skilled in the analysis of alternative proposals, then the process of legislative debate and political decision may well be adequate to deal with questions of balanced development. But many less developed countries have no such historical experience to guide them. (They lack most or all of the above). In these circumstances Governments have been interested in finding guidance in the experience of other countries (United Nations 1961: 38-9].

This, ultimately, is the argument for including an extensive range of social and economic development indicators for all countries in each edition of the HDR, so that every measurable dimension can be considered in detail.

The combination of various economic and social indicators in a single index, such as the Human Development Index (HDI), is entirely another matter, as is the question of how much new information might actually be contained in the plethora of statistics which are published extensively each year.[21] As noted above, the UN study takes the view that 'in-so-far as the level of living is measurable, it must be expressed, not as a single quantity, but as a pattern of non-convertible quantities' presumably because there is no evident value system to suggest how we should add together separate measures of the gross domestic product, school enrolment and infant mortality. It is of some interest to note, therefore, that, while Anand and Sen (1994a) support the views on this point which are expressed in the 1961 UN study, the HDI methodology, as explained in Anand and Sen [1994b], flies in the face of this logic. In an attempt to resolve this apparent contradiction, Anand and Sen have suggested that:

> the efficacy of (the HDI) lies in providing an alternative *general* focus of attention – alternative to the ubiquitous GNP per capita. This is an exercise in presenting an alternative immediate view of the overall situation in a country or a region – a situation that may be very badly reflected by GNP statistics. On the other hand, to go beyond that into a fuller analysis of the situation of human development in that country or region, *it is quite essential to step over the HDI on to the more detailed information provided in the HDRs* (Anand and Sen 1994a: 18, emphasis added)[22].

Anand and Sen (1994a) are significantly more critical than the authors of the 1961 UN study of the potential misuse of national income statistics. The latter submit that:

> the closest approach to a comprehensive measure of economic and social development is the per capita national income. (However, this) is not an adequate aggregate from

> a social point of view, and cannot be regarded as a satisfactory comprehensive measure of social welfare (United Nations 1961: 38).

This criticism is mild when compared with Anand and Sen (1994a: 17) as quoted above, who go on to argue that:

> the reliance on a standard measure of economic progress such as the growth of GDP not only specifies an evaluative space (the world of commodities – irrespective of their distribution and use) but also particular weights to be put on the respective commodities. For example, the use of market prices for the purpose of weighting – in calculating real income or real consumption – amounts to attaching the same weight per dollar to the rich person's many dollars as to the poor person's meagre means.
>
> This 'completeness' is often seen as an advantage of the traditional GNP-centred measures of progress. Certainly, it reduces the *need* for social values, but for the same reason, it also eliminates the *opportunity* for conscious social valuation ..... In contrast, the specification of an evaluative space in the form of conditions of living, even when supplemented by some indicators of economic means such as the GNP, leaves the analyst the freedom to decide what weights would be most appropriate for the exercise in which he or she might be engaged. *It is on this major shift of the information focus that the rationale of the human development approach has rested.* (Anand and Sen 1994a: 17, final emphasis added).

Two comments on these criticisms might be appropriate here. One obvious point to make is that these are criticisms of the GNP as a measure of welfare, and, as such, are directed at what I have previously suggested is an inappropriate interpretation of measures of the domestic product. They are not valid criticisms of GDP as a measure of output or of GNP as a measure of income generated by production. The criticism amounts, therefore, to nothing more than a grumble over the inappropriate use of particular statistics, not a *critique* of the statistics *per se.* In constructing a measure of product, it is entirely appropriate that a banana should be counted as having the same value whoever might eat it. A second more worrying point is that, the force with which Anand and Sen present their case notwithstanding, there is no instance that I am aware of within any of the HDRs, that have been published to date, in which a particular problem is analysed using carefully-crafted weights which have been deliberately chosen to illuminate the task at hand. By implication, the 'opportunity for conscious social evaluation' to replace market evaluation is one that the HDRs have not as yet exploited in practice, other than in the selection of subject matter and supporting evidence. Nor is there any prospect that this opportunity might be exploited in future, since the architects of the HDRs commend them as a 'reassertion of the classic humanist approach' (Anand and Sen 1994a: 18) which is not a sufficient foundation on which to build a system of measurement or even for identifying a strong ordering of options. One must begin to worry, therefore, that not only does the HDR approach apparently reject a role for the market in generating information which is a useful input into 'conscious social evaluation', of resource costs, for example, but also that it is not leading to an alternative calculus of costs and benefits which can be used instead of accounting prices.

Anand and Sen place great store in their analysis on the distinction between means and ends and emphasize this by labelling a concern for economic growth as 'the opulence approach', only to concede subsequently that their characterization is less than fair. Similarly, they castigate an exclusive concentration on people as 'human capital', which would be relevant if anyone was intent on doing that. Can we not all agree that the sense in which people are an embodiment of human capital is an aspect of their being, not the whole *persona*.?[23] It would, perhaps, be the only aspect that mattered to the owner of a slave, that is, when freedom is denied. But, otherwise, freedoms are of the essence, and one of the more constructive aspects of the paper by Anand and Sen (1994a) is their rehearsal of the arguments for creating freedoms and choices as the primary focus of development policy, a theme which Sen has been at pains to clarify over the years and one which has resonated through all the HDRs to date.

Another, less familiar theme concerns the question of sustainability, and what we might mean by that. In developing their position, Anand

and Sen (1994a) make the point that sustainability should not be defined in such a way that no irreversible investment decisions can be made or that it is invariably wrong to deplete natural resources. In this they invoke the support of Solow (1991) in arguing that what is at stake is a general responsibility to maintain opportunities for future generations that are no less than those that we enjoy today, even though some specific choices or freedoms may have been lost in the meantime. This, of course, begs the question of deciding on a value system which allows one freedom or choice to be traded off against another since the possibility of a weak ordering of consumption baskets is implicit in any attempt to make this argument more precise. It also assumes something about our understanding of nature, since we do not have complete knowledge of what is being lost when a forest is converted to arable land or whether such a process must always be irreversible.

A second point in the Anand and Sen formulation is that optimal growth does not guarantee sustainability. This also raises some difficulties, since sustainable development is defined, for the purposes of their demonstration, as an intertemporal growth path along which the first derivative of a scalar measure of well-being is non-negative. It is implicit, therefore, that a value system might exist according to which the components of well-being can be added up. We are not told what this value system might be, however.

Stepping over these difficulties (to borrow a phrase), the problem of deciding what sustainability might mean operationally is addressed by Anand and Sen as an aspect of their broader concern for universalism, which they promote as an essential element of human development: 'the demand of sustainability is, in fact, a particular reflection of the universality of claims – applied to the future generations vis-à-vis us.' (Anand and Sen 1994a: 1). However, one should perhaps add that in this case there is a particularly Rawlsian flavour to the argument since there is an edge to the universality of claims which suggests that we should be most concerned with whichever generation, including our own, is likely to find itself in the most reduced circumstances. A legitimate implication then seems to be that if one has great faith in technical progress, then perhaps we should worry less about the sustainability of our life-styles. It is far from obvious that this is an area in which humanist values are going to help, which is, perhaps, one of the reasons why most of us are less sure about how we should react to environmental concerns than we are about vegetarianism.

If the problem of sustainability has to remain on the agenda of unresolved issues, this does not detract from the importance of universalism or, what I would prefer to call 'inclusivity', for the design of a human development strategy. If we each care for one another and act on this directly or through a social structure of caring institutions, then it is apparent that any one individual or group is less likely to be left out of the development process and the chances of achieving growth with equity are enhanced accordingly. It is also the case that societies which marginalize a significant number of their members run the risk of being disrupted by violent means if the prevailing (democratic) institutions are unable or unwilling to bring about whatever reforms may be necessary to preserve social cohesion. There is a case, therefore, for the rich to support the inclusion of the poor out of their own self-interest. Concern for their welfare is essential for a healthy civil society, while a lack thereof constitutes a significant failure of public morality which can, in its own time, result in the dissipation of whatever potential there may otherwise have been for human development. History provides numerous examples and it could be important to learn these lessons.[24] The authors of the 1961 UN study note that the unique destiny of every nation is to be charged with creating a future out of its own particular past. But this should not, of course, preclude our learning the lessons that can be gleaned from the history of others.

3. Let all flowers bloom ?

In a powerful critique of the HDRs, Srinivasan (1994) has pointed to their divorce from standard methods of economic analysis, while Atu-rupane *et al.* (1994) have emphasized the many policy areas in which there is agreement between the HDRs, on the one hand, and the World Bank on the other.[25] In this final section I will make my own attempt at a reconciliation.

A useful starting point is to note the general agreement on the potential importance of an empirical approach, which offers the possibility for one country to learn from the experience of another, and for all developing countries to learn from the history of those that are classified today as being developed. But research in this area must break new ground if this potential is to be realized. It must allow, for example, that Sri Lanka might never have been an example that other countries either could or should have wanted to follow[26] and that the reasons for economic failure in Kerala are just as important as those which explain its successes on the social front. The chances of achieving this deeper understanding are slim for as long as analysis is confined to international comparisons based on the unreliable data that are made readily available by the multilateral development agencies.[27] What is needed most of all in this area is a series of studies in individual countries which attempt to provide a robust explanation of some critical features, such as the reduction of infant mortality, according to recognizable sociometric techniques.

It is in moving from the empirical to the *a priori* that the philosophy which underpins the HDRs might be seen as controversial. And this is not because of the avowed humanist perspective. Rather, it is because the 'humanitarians', as Streeton (1994) refers to those of like persuasion to himself, have no apparent place in their philosophy, as understood from their writings, for notions of Pareto optimality and opportunity cost. Accordingly, they have some difficulty in engaging in debate about the appropriate role of the market and entrepreneurship as a driving force in development.

This is not a matter of the *primacy* of markets or private enterprise. It is simply a matter of what role markets and private enterprise might be encouraged to play and where the limits of that role might properly be located. In suggesting earlier some ways in which the boundaries of economic analysis might be expanded with reference to time use, I am attempting little more than to build some theoretical foundations to support the similarities in UNDP and World Bank policy recommendations which have been noted by Aturupane *et al.* (1994). To the extent that these foundations are built on notions of consumer sovereignty and production efficiency, they are consistent with a broad class of social welfare functions. It is well known, of course, that particular Pareto optima may be irreconcilable with the current distribution of wealth and power in any one country. But it seems reasonable to infer that, if UNDP had wanted to argue within the HDR that this is their main concern in relation to most countries, then they would have done so by now. And if this is not the main concern in most countries, then perhaps it should be in some cases, of which Pakistan may or may not be one. Otherwise, in relation to countries in which the political preconditions for human development are more firmly established, the problem of deciding what the appropriate role for the market might be, given the current distribution of power and wealth, calls for an answer in the context of the *Human Development Report* because it is central to any continuing effort to narrow the gap between the world as it is and the world as it might be[28].

In the preface to *The Conditions of Economic Progress* Clark (1936) notes that, in relation to public affairs, economics is lexicographically dominated by politics, which is in turn dominated by history and, ultimately, by moral philosophy. It would, therefore, be wrong to take economic theory too seriously: the last word belongs elsewhere. But it would be equally wrong to infer from this proposition, which applies to all theory in the social sciences, that the calculus of economics has little to contribute. On the contrary, it sets an initial agenda that is useful because it helps to identify those areas in which market forces are in harmony with the concerns that all of us share for equity and freedom. It therefore helps to define the areas in which consensus might most easily be achieved. And economics is again useful when market forces are in conflict with other, higher-value systems because, while the economic calculus cannot tell us what the non-economic costs and benefits of some particular policy might be, it is often the case that the economic component is an important ingredient in decision-making.

Thus, the opportunity cost of defence is usually an important consideration in deciding how much defence expenditure to appropriate. In other words, the economic calculus provides a first approximation to what we might want to do that is often very useful.

In remaining ambiguous about the role of the market, the architects of the *Human Development Report* may unwittingly have invited the risk that economists could be tempted to extend the injunction to 'step over' the Human Development Index to the Report as a whole. The issue needs to be resolved because development is important. Hopefully, the balanced development formulation of a supply-side approach which has been outlined in this paper may be one way of proceeding towards a resolution. In attempting to improve on the first approximation that can be derived from the calculus, the approach may serve to advance the debate over the best ways and means of achieving (sustainable human) development.

Notes

1. The critical condition is that the rate at which foreign exchange earnings from exports are growing should be greater than the rate of interest that has to be paid on debt.

2. In Pyatt (1991) the 1980s are characterized as a 'wasted' decade.

3. The latest evidence on this point is to be found in Chen *et al.* (1994).

4. See the *Human Development Report* for 1992 (UNDP, annual from 1990) for evidence on this point.

5. See Cornia *et al.* (1987).

6. See UNDP (annually from 1990).

7. See UNDP (1992). Apart from Pakistan, the countries studied were Bangladesh, Colombia and Ghana. For Bangladesh and Colombia there are also reports available from UNDP which has provided summaries of these and the Pakistan report as annexes to Kaul and Menon (1993). Some of the ideas pioneered in these studies have since reappeared in Griffin and McKinley (1994).

8. The team included at various stages Ataollah Amini, Lee Bean, Dieter Berstecher, Tanguy de Biolley, Peter Bowden, Timothy King, David Monro, Paula Newberg, Omar Noman and Abdelmajid Tibouti. Tanguy de Biolley, Omar Noman and Timothy King helped me in preparing the final draft.

9. This might be seen, therefore, as a somewhat belated response to the World Bank Vice-President who claimed never to have seen a 'bankable gender project'.

10. See United Nations (1961). A subsequent document (United Nations 1964) reported on six country studies which were undertaken as a sequel to the 1961 report. The countries covered were

India, The Netherlands, Poland, Puerto Rico, Senegal and Yugoslavia.

11. An important source for these foundations is, of course, the HDR series itself. However, in some ways a better source is the Occasional Paper series being issued by the HDR Office of UNDP. One of these (Kaul and Menon 1993) has been referred to above. Others of particular interest are Anand and Sen (1994 a and b). Yet another illuminating source is Streeton (1994).

12. Some highlights of this literature are Sametz (1968), Nordhaus and Tobin (1972), Economic Council of Japan (1973), Eisner (1978 and 1989), Kendrick (1979), Jorgenson and Fraumeli (1989), Elson (1991) and Waring (1990).

13. Waring (1990) and Elsen (1991) have argued the general case. Chadeau (1992) and Goldschmidt-Clermont (1992) discuss possible corrections.

14. I argued this case for the first time in Pyatt (1990).

15. As yet there are no empirical studies which provide estimates of the relative sizes of these two 'halves'.

16. Pyatt (1992a and 1994) set out some details of this reformulation.

17. Note, however, that the poor typically cannot afford to satisfy their basic needs. Indeed, an inability to do so can be interpreted as a definition of poverty.

18. This is an idea that has a long pedigree, going back at least to Johnson (1964).

19. It is highly likely, if not certain that, from a demand-side point of view, one would want to raise transfers to the poor if the elimination of poverty is the immediate priority.

20. See Pyatt (1993) for an elaboration of the fiscal implications of the proposed reformulation.

21. Pyatt (1992b) argues this point which is taken up in McGillivray *et al.* (1995) and by Srinavasan (1994) in a swingeing critique of the HDI.

22. Streeton (1994) makes a similar point. For my own part, I am not persuaded by this neat footwork and regard the HDI as a distraction.

23. Perhaps we cannot, since Streeton (1994) writes at length about the difference between *human resource developers* and *humanitarians* as if these two groups were mutually exclusive.

24. They apply not only to developing countries but to developed countries as well. One wonders what the historians will eventually say of the changes wrought in the UK over recent years.

25. In this connection they particularly mention UNDP (1992).

26. The colonial history of Ceylon was unique while the post-colonial policies of the ethnic majority arguably were never entirely admirable.

27. The World Bank must take some responsibility for having lowered standards of data integrity with its early publications on income inequality. One might accept that it is admissible and even helpful to publish the only data we have, but it is not acceptable to then show little concern for the improvement of those data and to use them selectively to draw inferences which have little or no statistical significance. In this the *World Development Reports* published by the World Bank (World Bank, annual from 1978) has set an unfortunate precedent which the UNDP is now following.

28. At one point in its brief history to date, the HDI was complemented by a Human Freedom Index. However, this has now been withdrawn.

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