

ECO 563: Economic Development II (first half)

Department of Economics
Princeton University
Spring 2009

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All course materials will be posted on the class Web page at blackboard.princeton.edu.

1 Schedule

Class: 9 to 10:30 a.m. Tuesdays and Thursdays in B04 Fisher Hall.

Office hours: by appointment.

2 Course description

This is a graduate course in development economics. We will emphasize macro-level, general equilibrium outcomes: How poor or wealthy is a society? How equal or unequal? Why? The focus will be on methods of measuring and the role of the role of formal and informal markets in determining 1) the aggregate resources available for consumption at any date in time, and 2) the distribution of these aggregate resources among people in the economy.

3 Grading

The two course requirements are class participation and a five- to 10-page report on a paper or set of papers chosen in consultation with the instructor. The two requirements will be equally weighted in determining a grade.

I will base the evaluation of course participation on the extent to which you are familiar with the readings, as revealed by your participation in class discussion. I may also ask each student to present a paper or papers from the reading list, depending on enrollment.

You will write one report to satisfy the requirements for both halves of this course. You may choose a topic related to either the first or second half of the course. You must then consult with me or Professor Penny Goldberg, the instructor for the second half, about your choice of paper. You may replace the report with a detailed research proposal or short description of your own research, as long as it is relevant to the topics covered in the course. The report/paper is intended to get you started on critically evaluating existing work and conducting research on your own.

4 Tentative course outline

We will discuss papers marked with stars (★) in class. I have also listed a (far from exhaustive) selection of other relevant papers. In addition, because many of the topics we will discuss are important in macroeconomics more generally, the reading list includes some relevant papers from the literature on the U.S. economy; these are marked with daggers (†). The field exam at the end of the year may cover any paper listed below except those with daggers, as well as any other papers that I add to the list during the course.

1. Overview.

a. Aggregate growth facts.

- ★ Mankiw, N. Gregory, David Romer and David N. Weil, 1992. “A Contribution to the Empirics of Economic Growth.” *Quarterly Journal of Economics* 107(2), 407-437.
 - ★ Klenow, Peter J., and Andrés Rodríguez-Clare, 1997. “The Neoclassical Revival in Growth Economics: Has It Gone Too Far?” In B. Bernanke and J. Rotemberg, eds., *NBER Macroeconomics Annual 1997*, pp. 73–102, Cambridge, Mass.: MIT Press.
 - ★ Pritchett, Lant, 1997. “Divergence, Big Time.” *Journal of Economic Perspectives* 11(3), 3-17.
 - ★ Easterly, William, Michael Kremer, Lant Pritchett and Lawrence H. Summers, 1993. “Good policy or good luck? Country growth performance and temporary shocks.” *Journal of Monetary Economics* 32, 459-483.
- Hall, Robert E., and Charles I. Jones, 1999. “Why Do Some Countries Produce So Much More Output Per Worker Than Others?” *Quarterly Journal of Economics* 114(1), 83-116.

2. Measurement.

a. Inequality.

- ★ Sen, Amartya, 1997. *On Economic Inequality*, expanded edition. Oxford: Oxford University Press. Chapters 2 and A.1-A.5.
- Atkinson, Anthony B., 1970. “On the Measurement of Inequality.” *Journal of Economic Theory* 2, 244-263.
- Atkinson, Anthony B., and Andrea Brandolini, 2001. “Promise and Pitfalls in the Use of ‘Secondary’ Data-Sets: Income Inequality in OECD Countries as a Case Study.” *Journal of Economic Literature* 39, 771-799.

Deaton, Angus S., 1997. "Welfare, poverty, and distribution." Chapter 3 in *The Analysis of Household Surveys* (Washington: World Bank).

b. Poverty.

- ★ Sen, Amartya, 1976. "Poverty: An Ordinal Approach to Measurement." *Econometrica* 44(2), 219-231.
- ★ Elbers, Chris, Jean O. Lanjouw and Peter Lanjouw, 2003. "Micro-Level Estimation of Poverty and Inequality." *Econometrica* 71(1), 355-364.
- ★ Deaton et al., 2006, "An Evaluation of World Bank Research, 1998-2005," pp.59-63, and "Response from Development Research Group" (all available at <http://go.worldbank.org/U6VB0007X1>).
- Atkinson, A.B., 1987. "On the Measurement of Poverty." *Econometrica* 55(4), 749-764.

c. Price indexes.

- ★ Diewert, W.E., 1976. "Exact and Superlative Index Numbers." *Journal of Econometrics* 4, 115-145.
- ★ Deaton, Angus, 2006. "Purchasing power parity exchange rates for the poor: using household surveys to construct PPPs." Manuscript, Princeton University.

d. National accounts.

- ★ Deaton, Angus, and Alan Heston, 2008. "Understanding PPPs and PPP-based National Accounts." NBER Working Paper No. 14499.
- ★ Johnson, Simon, Will Larson, Chris Papageorgiou and Arvind Subramanian, 2008. "At Your Own Risk: Health Warnings for Growth Data." Manuscript.

3. Growth and inequality.

a. Does aggregation work?

- ★ Banerjee, Abhijit V., and Esther Duflo, 2005. "Growth Theory Through the Lens of Development Economics." In Aghion, Philippe, and Steven Durlauf, eds., *Handbook of Economic Growth*, volume 1A, pp. 473-552.
- ★ Banerjee, Abhijit V., and Esther Duflo, 2003. "Inequality and Growth: What Can the Data Say?" *Journal of Economic Growth* 8, 267-299.
- Kuznets, Simon, 1955. "Economic Growth and Inequality." *American Economic Review* 45(1), 1-28.

b. Models of growth and inequality.

- ★ Harris, John R., and Michael P. Todaro, 1970. "Migration, Unemployment and Development: A Two-Sector Analysis." *American Economic Review* 60(1), 126-142.
- ★ Greenwood, Jeremy, and Boyan Jovanovic, 1990. "Financial Development, Growth, and the Distribution of Income." *Journal of Political Economy* 98(5), part 1, 1076-1107.
- Aghion, Philippe, and Patrick Bolton, 1997. "A Theory of Trickle-Down Growth and Development." *Review of Economic Studies* 64, 151-172.
- Banerjee, Abhijit V., and Andrew F. Newman, 1993. "Occupational Choice and the Process of Development." *Journal of Political Economy* 101(2), 274-298.
- Benabou, Roland, 1996. "Inequality and Growth." *NBER Macroeconomics Annual 1996*, 11-74.
- Galor, Oded, and Joseph Zeira, 1993. "Income Distribution and Macroeconomics." *Review of Economic Studies* 60, 35-52.
- Lloyd-Ellis, Huw, and Dan Bernhardt, 2000. "Enterprise, Inequality and Economic Development." *Review of Economic Studies* 67, 147-168.
- † Buera, Francisco J., 2006. "Persistency of Poverty, Financial Frictions, and Entrepreneurship." Manuscript, Northwestern University.
- † Evans, David S., and Boyan Jovanovic, 1989. "An Estimated Model of Entrepreneurial Choice under Liquidity Constraints." *Journal of Political Economy* 97(4), 808-827.

4. Saving, self-insurance and insurance.

a. Facts and models.

- ★ Deaton, Angus, and Christina Paxson, 1994. "Intertemporal Choice and Inequality." *Journal of Political Economy* 102(3), 437-467.
- ★ Paxson, Christina H., 1992. "Using Weather Variability to Estimate the Response of Savings to Transitory Income in Thailand." *American Economic Review* 82(1), 15-33.
- Deaton, Angus, 1991. "Household Saving in LDC's: Credit Markets, Insurance, and Welfare." Research Program in Development Studies discussion paper No. 153, Princeton University.
- Deaton, Angus, and Christina H. Paxson, 2000. "Growth and Saving Among Individuals and Households." *Review of Economics and Statistics* 82(2), 212-225.

† Hall, Robert E., 1978. “Stochastic Implications of the Life Cycle-Permanent Income Hypothesis: Theory and Evidence.” *Journal of Political Economy* 86(6), 971-987.

† Zeldes, Stephen P., 1989. “Consumption and Liquidity Constraints: An Empirical Investigation.” *Journal of Political Economy* 97(2), 305-346.

b. Tests of full insurance.

★ Townsend, Robert M., 1994. “Risk and Insurance in Village India.” *Econometrica* 62(3), 539-591.

★ Mazzocco, Maurizio, and Shiv Saini, 2007. “Testing Efficient Risk Sharing with Heterogeneous Preferences.” Manuscript, UCLA.

Ravallion, Martin, and Shubham Chaudhuri, 1997. “Risk and Insurance in Village India: Comment.” *Econometrica* 65(1), 171-184.

Townsend, Robert M., 1995. “Consumption Insurance: An Evaluation of Risk-Bearing Systems in Low-Income Economies.” *Journal of Economic Perspectives* 9(3), 83-102.

Townsend, Robert M., 1995, “Financial Systems in Northern Thai Villages.” *Quarterly Journal of Economics* 110(4), 1011-1046.

† Cochrane, John H., 1991. “A Simple Test of Consumption Insurance.” *Journal of Political Economy* 99(5), 957-976.

† Hayashi, Fumio, Joseph Altonji and Laurence Kotlikoff, 1996. “Risk-Sharing between and within Families.” *Econometrica* 64(2), 261-294.

† Mace, Barbara J., 1991. “Full Insurance in the Presence of Aggregate Uncertainty.” *Journal of Political Economy* 99(5), 928-956.

† Schulhofer-Wohl, Sam, 2007. “Heterogeneity, Risk Sharing and the Welfare Costs of Idiosyncratic Risk.” Manuscript, Princeton University.

c. Sources of insurance and self-insurance.

★ Rosenzweig, Mark R., and Oded Stark, 1989. “Consumption Smoothing, Migration, and Marriage: Evidence from Rural India.” *Journal of Political Economy* 97(4), 905-926.

★ Rosenzweig, Mark R., and Kenneth I. Wolpin, 1993. “Credit Market Constraints, Consumption Smoothing, and the Accumulation of Durable Production Assets in Low-Income Countries: Investments in Bullocks in India.” *Journal of Political Economy* 101(2), 223-244.

★ Udry, Christopher, 1994. “Risk and Insurance in a Rural Credit Market: An Empirical Investigation in Northern Nigeria.” *Review of Economic Studies* 61(3), 495-526.

Fafchamps, Marcel, and Susan Lund, 2003. "Risk-sharing networks in rural Philippines." *Journal of Development Economics* 71, 261-287.

Udry, Christopher, 1995. "Risk and Saving in Northern Nigeria." *American Economic Review* 85(5), 1287-1300.

5. Capital and financial markets.

a. Financial deepening.

- ★ Burgess, Robin, and Rohini Pande, 2005. "Do Rural Banks Matter? Evidence from the Indian Social Banking Experiment." *American Economic Review* 95(3), 780-795.
- ★ Fulford, Scott, 2009. "Financial access in buffer-stock economies: Theory and evidence from India." Manuscript, Princeton University.
- ★ Townsend, Robert M., and Kenichi Ueda, 2006. "Financial Deepening, Inequality and Growth: A Model-Based Quantitative Evaluation." *Review of Economic Studies* 73, 251-293.

b. Investment constraints.

- ★ Banerjee, Abhijit V., and Esther Duflo, 2004. "Do Firms Want to Borrow More? Testing Credit Constraints Using a Directed Lending Program." Manuscript, MIT.
- ★ Banerjee, Abhijit, and Kaivan Munshi, 2004. "How Efficiently is Capital Allocated? Evidence from the Knitted Garment Industry in Tirupur." *Review of Economic Studies* 71(1), 19-42.
- Paulson, Anna L., and Robert Townsend, 2004. "Entrepreneurship and financial constraints in Thailand." *Journal of Corporate Finance* 10, 229-262.
- † Holtz-Eakin, Douglas, David Joulfaian and Harvey S. Rosen, 1994. "Sticking It Out: Entrepreneurial Survival and Liquidity Constraints." *Journal of Political Economy* 102(1), 53-75.
- † Lamont, Owen, 1997. "Cash Flow and Investment: Evidence from Internal Capital Markets." *Journal of Finance* 52(1), 83-109.