Some basic facts about the world

- Income dispersion between rich and poor countries
- What is GDP per capita?
  - US GDP per capita in 2009 is $49,900
  - Mexico? $8,143
  - Kenya? $738
  - Niger? $352
- These are all in actual US dollars. Adjusting for purchasing power differences makes some difference, but not much.
Even worse if you look over past 140 years

- USA vs. poorest countries was a factor of 10-1 in 1870
- USA vs. poorest countries was a factor of 45-1 in 1990

<table>
<thead>
<tr>
<th>Year</th>
<th>USA (F$)</th>
<th>Poorest (F$)</th>
<th>Ratio of GDP per capita of richest to poorest country</th>
<th>Average of seventeen “advanced capitalist” countries</th>
<th>Average LDCs from PWT5.6 for 1960, 1990 (imputed for 1870)</th>
<th>Average “advanced capitalist” to average of all other countries</th>
<th>Standard deviation of natural log of per capita incomes</th>
<th>Average absolute income deficit from the leader</th>
</tr>
</thead>
<tbody>
<tr>
<td>1870</td>
<td>2063</td>
<td>250</td>
<td>8.7</td>
<td>1757</td>
<td>from Maddison (1995)</td>
<td>2.4</td>
<td>.51</td>
<td>.64</td>
</tr>
<tr>
<td>1960</td>
<td>9895</td>
<td>257</td>
<td>38.5</td>
<td>6689</td>
<td>Average of seventeen “advanced capitalist” countries</td>
<td>4.2</td>
<td>.88</td>
<td>1.81</td>
</tr>
<tr>
<td>1990</td>
<td>18054</td>
<td>399</td>
<td>45.2</td>
<td>14845</td>
<td>Average LDCs from PWT5.6 for 1960, 1990 (imputed for 1870)</td>
<td>4.5</td>
<td>1.06</td>
<td>3.16</td>
</tr>
</tbody>
</table>

Notes: The estimates in the columns for 1870 are based on backcasting GDP per capita for each country using the methods described in the text assuming a minimum of P$250. If instead of that method, incomes in 1870 are backcast with truncation at P$250, the 1870 standard deviation is .64 (as reported in Figure 1).
Why could this be?

- Gap between richest and poorest countries is enormous, and the gap is growing
- Why could this be? What’s different between these countries?
- Let’s make a list:

  Some hypotheses:
  - Geography: temperature, disease burden
  - Human capital: education
  - Physical capital
  - Institutions: democracy, corruption, etc

- What does the data say? Let’s start by looking just at some cross-sectional graphs
What do we learn from all these graphs?

- Rich countries seem to be better on all of these dimensions
  - Geography
  - Human capital
  - Institutions

- These graphs don’t necessarily tell us that these factors cause the income differences. Why not?
This course is going to explore the role of politics and institutions in developing countries.

We’ll explore both whether political institutions matter for development, and if so, how to analyze political institutions in developing countries.

Let me give a preview of where we’re going.
Does political economy matter? And how do we know?

- The cross-sectional graphs we showed suggests that there is a correlation between political institutions and economic development.
- But do politics actually affect development?
- Many countries have become wealthy without having democracy (e.g., China, Singapore) and some countries became wealthy first, and then became democratic (e.g., Korea).
- How do we know if political institutions actually affects development?
- We’ll study several recent empirical studies that explore whether there really is a link.
  - Do political leaders matter? Does it matter who the President is?
  - Do historical institutions matter? 50 years after the end of colonialization, do colonial institutions still matter for development? Do even older institutions still make a difference?
Voting and Policy Determination in Democracies

- How to think about elections:
  - The benchmark is called the "Median Voter Theorem." The basic idea is that you win elections if you get > 50% of the vote. This says that if candidates compete, then policies should express the preferences of the median voter.

- Does this hold in practice? Why or why not?
  - Maybe politician’s identity matters (e.g., women, minorities, etc)
  - Maybe people vote based on what happened in the past, not the future
  - Maybe people vote for good politicians, not just whatever policy they most prefer
  - Maybe people just vote for whoever will bribe them the most
  - Maybe with more than 2 choices, things get a bit more complicated than the median voter theorem suggests

- Common theme we’ll explore: how does the way that voting takes place in developing countries influence the policies that governments actually put in place and ultimate development outcomes
Dictatorship and Democracy

- Does democracy become more likely with income?
- Can dictators do whatever they want? Why or why not?
- Why are there often elections in dictatorships?
Collective Action

- Not all public goods are provided by the state. In many cases, people do it themselves.
- This is true in the US to some degree (from PTAs to citizen initiatives) but even more so in developing countries.
- Topics we’ll discuss:
  - The benchmark in economics is the free-rider problem – why should I pay when someone else will?
  - Is this problem worse in ethnically diverse settings?
  - What are the implications for monitoring officials to make sure they do their job?
Wars are a challenge to the state, either from outside or within.

One view is that wars shouldn’t happen in equilibrium.

- They are very costly.
- So both sides should figure out who would win the war, and have transfers from the would-be loser to the would-be winner and avoid all the costs.

Yet they do happen.

- Why? Why might the logic I just outlined break down?
- We’ll then spend 2 lectures looking at civil wars, trying to understand what makes them more or less likely and how one can recover from civil wars.
Corruption can undermine the state’s authority in many ways

- Government officials can create hassles to get you to pay bribes
- Bribes allow law breakers to pay their way out of breaking the law – which can undermine the government’s ability to crack down on lawbreakers
- Theft from government projects can mean that government can’t execute projects it would like to
- etc.

We’ll ask four basic questions about corruption

- What are the impacts of corruption? Is corruption inefficient?
- How do corrupt officials respond to incentives?
- Can we think about corrupt politicians using the economics of firms?
- How do politicians use their influence to channel rents to favored friends and firms?
Pre-requisites

- I will expect you have taken the pre-reqs:
  - 14.01 (introductory micro)
  - 14.30 (statistics for economists)
  - or the equivalent

- If you have already taken 14.32 (econometrics), that’s will be helpful. However, we will not assume this material.

- If you’re not an MIT undergrad, or if you have questions, see me after class.
Course Details

- **Grading and assignments**
  - Problem sets (30%). There will be 5-6 problem sets, so one approximately every two weeks. These will be a mix of theoretical exercises and empirical exercises. You will need to use Stata to complete the problem sets. You must do these individually.
  - In-class midterm (30%). March 22.
  - Final exam (40%).
  - Class participation is expected, and will be taken into account in marginal cases.
14.75 Political Economy and Economic Development
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