Impaled on the trident of inflation and recession in the developed countries and much more expensive oil, world growth prospects have deteriorated in the past year. Higher oil prices have improved the outlook for the fifth of the developing world's population that lives in oil-exporting countries; their average GNP per person could grow at around 3.0 to 3.5 percent a year in the first half of the 1980s. But for the four-fifths that live in oil-importing countries, the first half of the decade will involve slower growth. For developing countries as a whole, growth will be substantially below that forecast in last year's Report.

Governments of oil-importing developing countries must take steps to reduce current account deficits and adapt to more expensive energy—and at a time when demand for their exports from industrialized countries has slowed, not just because of the rise in energy prices, but because of cyclical and structural problems as well. The GNP growth of oil-importing developing countries could thus fall to about 1.8 percent per person a year (the Low case). Prospects for the low-income oil importers would be particularly bleak in this scenario: income per person in low-income Sub-Saharan Africa would decline, and the number of people in absolute poverty in the developing world as a whole would increase.

This Low case (or an even worse outcome) could come about—but it need not. In the High case the oil-importing developing countries would grow at about 2.4 percent per person a year in 1980-85, and by 1990 there would be 80 million fewer people in absolute poverty than in the Low case. This would require that developing countries adjust successfully—cutting their external deficits by raising exports rather than lowering imports, while increasing both investment and efficiency in resource use. What the industrialized countries and capital-surplus oil exporters do is also vital—in stimulating demand for developing-country exports, in recycling oil surpluses and in providing aid. But even in the High case, the growth of income per person in the developing countries will not match that in the industrialized countries. Taking the steps needed not just to attain, but to exceed, the High case is thus the major development challenge of the next five years.

The success of the adjustment by developing and other countries to the economic circumstances of the early 1980s will not only largely determine their growth during that period but will also affect the chances of an acceleration of growth in the second half of the decade. With recovery in the industrialized countries and in world trade and with continued sound domestic economic policies, the oil-importing countries could grow almost as rapidly (3.2 percent) as the oil exporters (3.4 percent) and faster than in the 1970s. Without it, the growth of the oil exporters would be almost half a percentage point lower, and that of the oil-importing countries a full percentage point lower. Much of the first part of this Report has been about the policy decisions that will determine the actual outcomes, in both the near term and the longer term.

External factors

- Trade. The ability of developing countries to afford the imports they need for growth depends crucially on their exports to the industrialized countries, which currently constitute two-thirds of their market. The industrialized countries, even those determined to combat inflation by restraining growth, must minimize the effects their deceleration will have on the developing world. This means expanding the volume of imports, maintaining the relatively free trading opportunities that now exist for most products, and starting to lower the barriers against other goods of particular importance to developing countries, such as textiles, clothing, leather goods, electronics, steel and some agricultural commodities. To do so would increase the localized pains of structural change in the developed countries. But there are internal remedies for these pains, and liberalization of trade will pay off in faster productivity growth and lower inflation. The oil-
exporting nations can also help by rapidly expanding their imports from developing countries.

- Energy. The developing countries that import oil have been hard hit by the price explosion of the past 12 months and can expect their energy costs to rise further in real terms. At the same time, modernization of their economies will spur demand for energy; so they face a continuing need to adapt to the rising cost of imported oil. They will find this easier if oil-exporting countries can avoid supply disruptions and sharp price changes. More generally, the world economy will perform better if oil prices follow a smooth path; violent fluctuations play havoc with internal resource allocation and the external payments system. Reliable supplies and smooth price changes will be more likely if developed countries improve their energy conservation and develop alternative sources.

- Capital flows. Current account imbalances will be large in the next few years, again requiring special efforts to recycle finance to oil-importing countries, especially in the developing world. There is a serious risk that reluctance or inability to finance large external deficits will lead to levels of trade, investment and economic efficiency—hence, of growth—lower than anyone would wish. Even in the later years of the 1980s, when the severity of payments imbalances is expected to diminish, the growth of developing countries will continue to depend on inflows of foreign capital.

For the low-income countries, which can borrow little commercially, this means more aid. There is a real danger that the modest aid increases projected in this Report will not be achieved. In their own long-term interests, as well as those of the developing countries, both OECD and OPEC donors should make every effort to expand their aid relative to GNP, even in periods of domestic stringency. And they should concentrate their aid even more on low-income countries.

Commercial capital, mainly from banks but also from the bond market, private direct investment and official sources, will be available to help the middle-income countries. But not all countries will be well placed to borrow much more from private commercial sources; without additional financial assistance from other sources, their growth will slow down. In particular, there is not enough long-term program (non-project) finance to support the structural changes required in many countries. Some will benefit from the structural adjustment lending of the World Bank and assistance from the IMF; enlarged official flows of this sort, particularly from multilateral agencies, could and should play a larger role.

Internal factors

While powerfully influenced by the international environment, the progress of developing countries depends even more on their own policies and initiatives.

- Trade, energy and capital flows. In trade, the developing countries can use pricing and other policies to stimulate production of internationally traded goods—both exports and import substitutes; but they should avoid bias toward import substitution, since this reduces efficiency and discourages exports. With regard to energy, they, like the industrialized countries, can minimize the loss of real income caused by higher oil prices through conservation and greater domestic energy production. As to capital flows, they can take full advantage of their opportunities for prudent borrowing from commercial and bilateral lenders and multilateral institutions.

- Investment and production efficiency. In attracting (especially commercial) finance, and in speeding development more generally, trade and energy strategies play an important role. So do other policies that increase investment, improve administration, raise agricultural productivity and make better use of capital, labor, natural resources and imports.

- Human development. The internal factor on which this Report has focused is the human one: the role not only of education and training, but also of health and nutrition. In addition to the important direct benefits that programs in these areas confer, the Report stresses another aspect, long-standing but often neglected—the role of human development as investment, contributing to growth. The importance of technical, professional and managerial skills is well known. Less well known but firmly established by research is the importance of primary education, which affects the knowledge and attitudes of farmers and other workers.

Investment in human resources, like other kinds of investment, can be ineffectual unless complemented by other productive inputs and by policies to ensure that resources are efficiently used. Human development programs must also be carefully chosen and efficiently carried out. Despite these qualifications, there is strong evidence to support the commonsense proposition that human development can make a valuable contribution to growth.

Studies at the firm, farm and project level have shown that better education, health and nutrition can raise incomes and productivity, and that the economic rate of return to investment in schooling
is high, frequently well above that of physical investment. For primary schooling, the rates of return in a large group of countries average more than 20 percent. At the aggregate level, cross-country comparisons show that developing nations with higher literacy rates have grown faster, even when allowances are made for other influences on growth and for reverse causation—the effect of growth on literacy. This finding is reinforced by case studies and historical evidence.

- Population. One important way in which human development contributes to raising average incomes, as well as to other social goals, is by reducing population growth. Reducing fertility is not an end in itself; but lower population growth in most developing countries tends to result in greater investment per person in physical capital and human skills—and thus in faster growth. Better nutrition and health, by lowering infant mortality, are essential ingredients of fertility decline. So is education, especially of women, since it delays marriage, alters attitudes about family size and makes modern contraception more acceptable. Increases in income themselves are a cause, as well as a consequence, of reduced fertility: people who are less poor have good reasons for wanting fewer children (including less need for their labor and for support in old age). And research has confirmed that family planning programs also are important in bringing about slower population growth.

**Human development and poverty**

Human development can thus assist growth. But the Report has stressed even more its potential contribution to reducing absolute poverty.

- Growth and poverty reduction. Growth is vital to reducing all aspects of absolute poverty—malnutrition, ill health and illiteracy, as well as low income—especially in the poorest countries. But growth unaccompanied by other measures may neither boost the incomes of the poor much, nor lead to much progress on nonincome aspects of poverty. On both counts, human development programs have a part to play.

- Raising the incomes of the poor. The Report has discussed a wide range of policies, many of which positively reinforce growth, that can help raise the incomes of the poor. Support of agriculture, land and tenure reform, policies to raise the demand for labor, and the various kinds of research are four important areas considered. Human development is an essential complement. It accelerates the spread of new techniques to small farms and increases the opportunities of the poor for employment in the modern sector. And because fertility and family size are reduced, the earnings of adults do not have to be spread so thinly among children and other dependents.

- Nonincome aspects of poverty. The worst aspects of absolute poverty include not only low income, but also malnutrition, frequent child death, disease and ignorance. All can be helped by human development programs. Less obviously, there is a complex interdependence between the different facets of human development—as there is between human development and increases in income. Health, nutrition, education and fertility all affect each other. Most striking, partly because least expected, are the powerful effects that education, especially female education, has on fertility, child health and nutrition. As this suggests, human development is a circular process, one that can be vicious or virtuous, according to circumstances and policies. And it has its own momentum: what is done (or not done) today powerfully influences what can be done a decade or more ahead.

- Practical aspects of human development. Human development is easier said than done. But much has been learned about the comparative efficacy of different policies and programs. In nutrition, for example, there is growing agreement that the central issue is not improving the balance between calories and protein but increasing the amount of staple foods the poor can afford; this involves raising their incomes, stimulating production of these foods and, in some cases, targeted subsidies. In health the vital role of primary care, together with education and control of mass diseases, is now generally acknowledged. In fertility there is better understanding both of how to implement family planning programs and of how such programs interact with socioeconomic and cultural conditions. In education more importance is now attached to its behavioral effects; and in raising educational standards, the significance of class size has been shown to be much less, and that of teaching materials much more, than was formerly believed.

Hard experience has also shown the difficulties of implementing human development and how to tackle them. Political obstacles such as urban bias, competition for resources, and the weak position of the poor often have to be overcome; but efforts to improve basic education, nutrition and health have a universal political appeal. The financial constraint on programs often appears binding; but frequently there are unexploited ways of cutting costs and harnessing additional resources. Human development programs can also
encounter serious administrative constraints; here it is important not only to improve administration but also to choose the most manageable mix of programs and to encourage local participation. More paradoxical, but equally vexing, is the gap between need and demand that can sometimes lead to underused schools and clinics or the underrepresentation of girls and women in human development programs. Experience suggests ways in which this gap can be narrowed, and in some cases bridged.

- Tradeoffs and choices. Planners have to choose at the margin between human development and other activities, and between different human development activities. The choices are not easy, nor should they be the same in all countries.

The economic payoff to human development eases the tradeoffs between growth and poverty reduction. But it does not eliminate them, which means that policy decisions will be affected by the relative emphasis attached to increasing growth, raising the incomes of the poor and attacking the nonincome aspects of poverty. And whatever the balance of objectives, the difficulty of quantifying costs and benefits often compounds the problems of deciding how large the human development budget should be, and how it should be divided among education, health, nutrition and family planning, as well as within each of these areas.

The way in which these dilemmas are resolved must vary according to the circumstances of each country. Political and social priorities are important. So are income levels and growth prospects, and past progress in human development. In considering human development and other steps to reduce poverty, the low-income countries of Africa and Asia, for example, must perforce put strong emphasis on economic returns.

Nothing can make widespread absolute poverty melt away overnight. And human development at best can only part of the job. Without effective policies on other fronts, and without active and enlightened support from the rest of the world, progress will be agonizingly slow. But these other policies will not be sufficient. The most valuable resource any country has is its people, the means and the end of economic advance.