1 Overview

The world economy is at a low ebb, weakened by difficulties in adjustment and by faltering growth in the major industrial countries. For much of the past thirty years, growing interdependence—through trade, capital, and migration—strengthened the forces of economic expansion and spread them around the world. But, as recent events have illustrated, these links can transmit problems from country to country just as surely as benefits. In the industrial countries, large fiscal deficits, tight monetary policies, and concern about inflation have raised real interest rates to unprecedented levels, curtailed growth, and depressed the export earnings of developing countries, contributing to severe liquidity problems for many of them. With their ability to buy imports and service their debt thus reduced, many developing countries have had little alternative in the short term but to reduce growth.

In this year’s Report the discussion of the international economy and the prospects for growth is arranged in three chapters. Chapter 2 reviews the measures taken by various groups of countries to cope with the sudden and large shocks to the world economy during the 1970s. It concludes that most developing countries adjusted better than the industrial countries over the 1974–81 period. But the low-income countries have been particularly hard hit by the recession in the industrial countries.

Chapter 3 describes the development achievements of the past three decades—a period of unparalleled economic growth, but growth which was spread very unevenly around the world. Growth was particularly slow in the poorest countries; even there, though, tremendous progress was made in improving the quality of life and establishing the preconditions for development.

Chapter 4 discusses the prospects for the 1980s in the light of recent events as well as longer-term trends. It emphasizes that, although international prospects have worsened over the past year, the middle-income countries should be able to continue their progress in narrowing the gap between themselves and the industrial countries. But the prospects for the low-income countries remain a matter of grave concern. India and China may not be able to sustain the progress they made in the 1970s without continued external assistance. In the other low-income countries, which are even more heavily dependent on aid flows, output growth is likely to remain severely depressed.

International issues and past development

During the 1970s the developing countries adjusted remarkably well to the more turbulent conditions in the world economy. Since 1973, they have grown roughly twice as fast as the industrial countries. Faced with sharply increased prices for their imports of fuel and manufactured goods, developing countries borrowed more, boosted exports, and substituted for imports. In many of them, investment rose as a proportion of GDP.

A rising level of investment and sustained growth are both cause and consequence of successful long-run adjustment. Most developing countries were able to make good use of their additional borrowing in the 1970s. For a time, rapid inflation and negative real interest rates eroded the nominal value of their debt-servicing obligations. Inflation is a mixed blessing, however. It causes debts to be paid off earlier, because nominal interest rates rise to reflect lenders’ anticipation of the lower real value of loan repayments in the future. About one-half of total developing-country medium- and long-term external debt carries variable interest rates. Much of the new debt contracted at fixed rates of interest has also incorporated expectations about future inflation. The heavier burden of repaying existing debt and the slowdown in net new borrowings caused by high interest rates has exacerbated the liquidity difficulties of many developing countries—and some of the countries of Eastern Europe. Since 1979, the rise in real interest rates has
also reduced the real value of the net resources transferred to developing countries.

Chapter 3 highlights the changing structure of the international economy over the past thirty years, with the emergence of new clusters of buoyant economic activity, notably in Japan and the Pacific rim of Southeast Asia, the Latin American economies, and the oil exporters centered around the Middle East. These changes became more conspicuous in the 1970s, as growth in North America and Europe slowed while a group of middle-income countries increased their investment and exports and maintained more rapid growth. The oil exporters and semi-industrial countries began to narrow the gap in relative terms between their per capita incomes and those of the OECD countries. The low-income countries, for the most part, remained on the periphery, lacking the energy resources or the manufacturing capacity to achieve rapid growth through trade. But helped by very high domestic savings, China and, to a lesser extent, India and Pakistan have significantly improved their per capita incomes. In many other cases, growth was hampered by the weak performance of agriculture, a weakness that grew more marked in sub-Saharan Africa in the 1970s.

Although growth requires an increase in the primary factors used in production, improvements in the efficiency of their use have been responsible for most of the growth in developing countries. In Africa, in particular, recent analysis suggests that the absolute amount of investment makes a less important contribution to economic growth than the way investment is allocated and used. There are many examples of countries where high rates of investment have failed to produce high growth rates.

In most developing countries, low- and middle-income alike, remarkable social progress was achieved over the past three decades. Literacy, health, and life expectancy not only reflect substantial gains made amidst extreme poverty, but also create their own momentum of growth. By broadening domestic technical and managerial skills, changing the attitudes of farmers and workers, and, it is hoped, lowering the birth rate, human development offers the prospect that per capita living standards can be improved faster in the 1980s. This long-term improvement in human capital is one bright spot that is shared by almost all developing countries.

Development prospects

Development prospects for the international economy, discussed in Chapter 4, have worsened over the past year. The list of reasons for pessimism is long: continuing recession in the industrial countries (which also heightens the threat of protectionist measures); the developing countries' adverse terms of trade and depressed export volumes; high and more volatile interest rates that limit borrowing; and large debt repayment burdens. If not soon overcome, these barriers to growth could condemn the world to the sluggish growth that is outlined in the World Bank's Low case. Developed from work with the Bank's global model, alternative scenarios illustrate some of the factors that will determine the pace of growth in the world economy. The High case illustrates the conditions for more rapid recovery from present difficulties.

For developing countries, the most salient features of an unfavorable international outlook for the 1980s are less aid, continued weakness in commodity prices, deteriorating export opportunities, and poor prospects for commercial borrowing. The first two factors are comparatively more serious for low-income countries—and there is very little they could do about them in the near future. The other two would hurt middle-income countries more; but appropriate policy responses—flexibility in policies toward trade and industry, plus internal adjustments to enhance creditworthiness—would mitigate their harm.

The Low case growth rates are clearly inadequate in the light of the developing countries' past performance as well as their potential, expectations, and needs. Even among the major exporters of manufactures and the oil exporters, unemployment and underemployment have characterized all but a few of the fastest growing economies. Should the Low case come about, the social and political tensions created by rising unemployment would seriously complicate the tasks of economic management.

The Low and High cases are neither forecasts of what will happen nor firm boundaries of feasible outcomes. They are, at best, likely outcomes under combinations of either reasonably good or relatively undistinguished policies in the developing countries themselves, and of policies in developed countries that are either fairly helpful toward growth and development or rather unhelpful. If the slow-growing countries were to emulate the average growth achieved in the past, while those which had had average growth rates were to match the fastest growers, even the High case projections could be comfortably exceeded. The final outcome cannot be forecast because it is not pre-
Priorities for industrial countries are, first, the restoration of their own economic health and continued growth. But the maintenance of a liberal environment for trade and capital flows is essentially their responsibility as well. Although external finance accounts for only 13 percent of the total investment in developing countries (or 4 percent of world savings), it makes an important contribution by providing essential imports of machinery, materials, and technology. It also helps cushion balance of payments shocks. To facilitate greater capital flows, aid must not be allowed to suffer from pressures to cut fiscal deficits.

The experience of the 1970s suggests that most developing countries have weathered the dislocations with remarkable discipline. Nevertheless, policymakers need to continue to stress the importance of several factors: increasing levels of domestic savings and investment, improving efficiency in the use of capital, and responsible management of external debt. To lay the foundation for development over the longer term, however, attention must be given to strengthening economic management and to developing a strategy for the 1980s. With very few exceptions, developing countries would gain significantly by giving greater priority to agriculture. This is the theme of the second part of the Report.

**Agricultural development**

The character of world agriculture has changed dramatically during the past thirty years. In the developed countries, scientific research together with the increased use of industrial technology, chemical fertilizers, and machinery have revolutionized production and marketing. Elements of this revolution have been adapted to many developing countries, but the variety of their circumstances—climate and environment (and the availability of technology appropriate to them), institutions, management, and policy—has produced widely differing performance and progress. Contrasts between the agriculture of developed and developing economies are illustrated in Figure 1.1.

The discussion in Part II is organized in four chapters. They deal with:

- The links between agricultural growth and overall economic development
- The sources of growth and...
their application in differing circumstances

- Rural poverty and food security
- Policy considerations and conclusions.

Agriculture and economic growth

In the past three decades agricultural output has increased at twice the rate of earlier periods. For the developing countries, these aggregates conceal large regional and intracountry differences. In most poor countries population growth sharply reduced the benefits—for low-income countries as a group to a modest 0.2 percent a year per capita over the 1960s—and per capita agricultural and food output declined in the 1970s. The poor of the low-income countries still face a severe food problem.

Agriculture dominates low-income economies, 70 percent of whose population depends on it. Its growth in large part dictates the growth of their GDP. The mass of the population spends 60 to 70 percent of its income on food, while many nonagricultural activities depend on agriculture—not least government itself, through its agricultural tax base.

As development proceeds, agriculture’s role diminishes, eventually accounting for a small fraction of both output and employment at advanced stages of development. For most developing countries, however, it remains critical, because its progress determines the speed at which countries can industrialize. In general terms, cost-reducing innovation and investment are central to speeding up agricultural growth. The benefits of productivity gains are partially transferred to consumers, because low food (and other commodity) prices stimulate the rest of the economy, while keeping it supplied with labor leaving the land for more productive employment.

One point emerges very clearly from the diversity of experience of the developing countries: rapid growth in agriculture and in GDP go together. Where the pursuit of industrialization—the favored target of planners in the 1950s and 1960s—has been successful, agricultural progress has not been sacrificed. Success in agriculture strengthens and helps sustain the momentum of the whole economy. Of equal importance is the contribution of sustained agricultural growth to the reduction of poverty.

The balance of interests between producers and consumers is the central issue of agricultural policy, and one governed by pricing structures. In the pursuit of goals other than agriculture’s development, developing-country planners have often tilted their pricing policy against agriculture—and paid a heavy price in lost agricultural growth. Incentives to farmers to invest and produce is a key stimulant to agricultural growth.

By contrast, the industrial countries protect agriculture to maintain some parity in incomes between farmers and other workers. This protection is extremely expensive—unnecessarily so, since it has spurred increases in agricultural output beyond economically justified levels and has seriously distorted international comparative advantage.

For policymakers, the challenge is to adjust domestic policies and to build a trading system in which comparative advantage can play a greater role in production. Faster progress on this front is clearly desirable to enlarge the developing countries’ access to markets and, in the long run, to ensure that the world’s agricultural resources are more efficiently used to increase per capita supplies of food.

The sources of growth

The tie between agriculture and nature distinguishes farming from most other activities. Innovation and investment have to be related to the specific environmental contexts. For example, the leading role of water control (irrigation, drainage, flood control) in populous Asia contrasts with the emphasis on basic infrastructure in some areas of Latin America and Africa, where land is ample. The public sector plays a dominant role in providing both infrastructure and large-scale irrigation systems, and faces special problems of management and financing in operating them. It also takes the lead in biological research, whereas mechanical and chemical innovations are dominated by the private sector.

No universal package of prescriptions can be offered. Nature, feasible cropping systems, available technology and the means to acquire and use it—they all vary too widely for any simple formula to make sense. However, a few lessons are clear.

- Investments in agricultural research, the result of both international and national initiatives, have paid off handsomely and have fueled growth during the past twenty years. The blending of basic science, applied research, practical experience, adequate incentives, and investment has yielded tremendous increases in output for certain crops, principally rice and wheat, in certain conditions. Given this high rate of return, investment in research should be not only maintained but accelerated. Specifically, it should be aimed at the hitherto neglected areas: rain-fed crops, root crops

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(cassava), and coarse grains (sorghum, millet), so as to boost productivity in humid and semiarid areas—particularly sub-Saharan Africa.

- Water control—largely irrigation but also drainage and flood control—is a major source of increased productivity. If a farmer is to adopt a new variety of seed and apply the right amount of fertilizer, he must be assured of adequate supplies of water delivered on time. Such assistance has generally provided high rates of return, though it requires considerable investment and strong local organization. Private sector irrigation, mainly by means of tubewells and small pumps, complemented the Green Revolution in South Asia. Where this technology can be applied, it remains an important factor in boosting agricultural output. In the future as in the past, however, the size and collective nature of the investments will require heavy reliance on public sector irrigation. In the larger irrigation systems, intelligent water management is a precondition for high productivity. Further investment in irrigation should go hand in hand with efforts to reform the management of the systems already completed and operating. The waste of scarce and expensive irrigation water remains very large.

- With urbanization and the growth of the cash economy, marketed food production will need to increase very rapidly. This will require considerable investments in crop storage, processing, and transport. Here especially, there is need for governments to consider carefully the respective roles of the public and private sectors in financing and managing those investments. Public schemes need continuous scrutiny to ensure that they are employed to best effect.

Efficient and equitable private sector performance needs effective government policies and administration.

**Rural poverty**

Worldwide, absolute poverty is overwhelmingly concentrated in the rural areas of developing countries. The 1980 Report estimated that 780 million people, excluding China and other low-income centrally planned economies, were living in absolute poverty. In China probably 150 million people live just above the poverty line. The one-fifth to one-quarter of the rural poor who are effectively landless have much the same income as very small farmers—close to bare subsistence—but they are more vulnerable to calamities and harder to reach with development programs.

Economic growth is the ultimate remedy for rural poverty. In fast-growing economies—mainly middle-income countries—absolute poverty has been greatly reduced as new employment was created off the farm, in both rural and urban areas.

Certain special initiatives will help reduce rural poverty and stimulate growth at the same time. Projects aimed at small farmers can boost productivity, especially if the projects are simple, focused on priority problems, and well integrated with government administration. Employment away from the farm also boosts incomes and has a direct relationship with agricultural prosperity. Agrarian reform that increases security of tenure can also increase productivity, and sometimes so can land reform, though most of the rural poor live in areas where farms are already small and land intensively used. Rural public works can reduce rural poverty, often very cheaply; by converting ample labor into needed capital, they help accelerate agricultural growth. The intensive involvement of the local population in the planning, execution, and financing of these initiatives plus sound design and good management appear to be the major determinants of their success.

Since the rural poor spend a large proportion of their budgets on food, they benefit as consumers from cost- and price-reducing agricultural development, especially if research is expanded on the crops they produce and consume. But food security for poor people will remain a priority for many years. This should include famine-related relief programs and schemes to reduce chronic undernutrition.

Without careful attention to targeting, food distribution programs to combat malnutrition often involve heavy budgetary costs—without necessarily doing much to improve nutrition among the rural poor. Governments should therefore consider whether these programs could not be better targeted and the resources saved then spent on direct investments in agriculture itself. Food subsidies are invariably politically charged, so governments may find it difficult to rearrange their budget priorities. But limiting distribution of subsidized food to the needy would cut the budgetary costs of subsidies without compromising their nutritional objectives.

**Conclusions**

For many years, the contribution of agriculture to growth and the capacity of traditional farmers to change were controversial and little understood issues. That is no longer so. Economic growth has gone hand in hand with agricultural progress. All farmers—small, medium, and large—respond to
economic incentives. Far from being "tradition-bound peasants," farmers have shown that they share a rationality that far outweighs differences in their social and ecological conditions. Farmers can contribute to agricultural investment. Even those farming only a few acres, save a substantial part of any extra income and invest it on their farms. They also use their own and their families' labor to level land, grow trees, dig ditches, and build paddy terraces—all activities that create the capital to produce more agricultural output in the future. Small farmers can be highly productive, typically producing more from each acre than large farmers do. Programs and policies favoring smallholders can thus offer good economic returns as well as increase employment and reduce rural poverty.

Given incentives and opportunity, farmers will expand output. That does not mean that governments and other official agencies should confine themselves solely to fixing those incentives. Research and technology need to be developed and adapted to local conditions. The lack of technological improvements suitable for African conditions is a main reason for Africa's poor performance so far. Internationally financed projects in agriculture are necessary to overcome obstacles, to demonstrate how to increase output, and assist in devising programs to benefit the poor. Major investments in irrigation, transport, and marketing networks are also needed, which require external assistance.

The constraints on agricultural growth do not lie in the behavior of farmers; they are willing to work hard, to adopt profitable innovations, or to invest for the future. Instead, the constraints are to be found in the environment in which farmers operate: the technology available to them, the incentives for production and investment, the availability and price of materials such as fertilizers, and the provision of irrigation.

The future thus depends on a number of factors—particularly the policy framework, advances in research, and the international environment. The proper incentive to farmers must be complemented by infrastructure. New research breakthroughs—especially for controlling tsetse fly and developing improved varieties of coarse grains, roots, and tubers—could open up and increase the productivity of vast areas. The international community can and should provide support.

Aid for agriculture increased in the 1970s, reflecting both a rising volume of aid in general and the increased share going to agriculture in particular. That in turn reflects changing perceptions among both donors and recipients about the role of agriculture and a clearer understanding of its importance in dealing with poverty. The experience of aid-supported agricultural development in the 1970s was in many cases novel. Aid helped finance a wider variety of programs and embraced more countries than ever before, forging new partnerships between donors and recipients. That past provides the spur for the future.