

Economic Development: A Case for Visionary Leadership

by Paul Weisenfeld

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Since 9/11/01, efforts to identify the causes of persistent poverty and despair in the developing world have expanded, largely focused on cultural factors, especially in Middle Eastern cultures. There is no question that cultural attitudes and practices have an impact on economic development. Culture, however, does not evolve in isolation. It is only one of many factors that impede economic growth. Geography, environment, and history influence the evolution of culture and have served as significant obstacles to growth in low-income countries. The failure to recognize these other factors leads us to underestimate the enormity of the challenges facing poor countries and, consequently, to devise prescriptions for overcoming poverty that are unrealistic and unlikely to succeed.

Prior to the eighteenth and nineteenth centuries, life for most Europeans and Americans who were not born into the landed elite was similar to that of the poor in the developing world today: nasty, brutish, and short. This was before the unprecedented creation of wealth brought about by democratic capitalism. In fact, Europe was the technological, cultural, and economic backwater of Eurasia for most of history, importing virtually all of its ideas and technologies from the Middle East and Asia. Europe's distinctive geography and history allowed for an era of increasing innovation between the fifteenth and eighteenth centuries, creating the conditions that ultimately transformed European culture and its American spin-off into the vibrant cultural and economic powerhouses of today. The Age of Discovery permitted the diffusion of technologies and ideas, creating an open, innovative atmosphere in Europe and a decentralized, competitive environment that further stimulated innovation and the growth of private business. Understanding these trends can help guide both the economic strategies of low-income countries and donor agencies' approaches. To overcome the

disadvantages of history, geography, and culture, poor countries require homegrown visionary leaders who heed the lessons of history.

With Open Arms: The Importance of Vigorous Contacts

A number of scholars, including Fernand Braudel, Jeffrey Sachs, Jared Diamond, and Robert Wright, have pointed to geographic conditions as determining factors in the different levels of development the world's nations have achieved. Sachs has focused on historic access to the seas and navigable rivers for trade and the prevalence of harsh tropical diseases as key determinants. Of the thirty most affluent countries in the world today, he notes, only two (Singapore and Hong Kong) are in tropical climates.¹ Similarly, Diamond has argued that favorable geographic conditions in Eurasia, as compared to subsaharan Africa, the Americas, and Oceania, allowed for the rapid spread of technology and ideas, which fueled increasingly complex development. The east-west orientation of Eurasia, with similar latitudes and relatively minor climatic variation, allowed for the rapid spread of crops, livestock, technology, ideas, and ultimately civilization.² Similar climatic conditions allowed the crops and livestock originating in the Fertile Crescent to spread east-west throughout most of Eurasia relatively rapidly and without much adaptation—despite the fact that Eurasia is the world's longest land mass.

By contrast, the predominantly north-south axes of subsaharan Africa and the Americas, entailing significantly greater climatic variation, acted as a barrier to the diffusion of crops and civilization. Deserts, mountain ranges, tropical forests, and the dearth of navigable rivers in these regions served as additional barriers to the diffusion of food production, technology, and ideas. While the Mississippi and Amazon certainly facilitated trade among native American peoples, the rain forests in the Panamanian isthmus, the tropical Amazon forest, and the northern Mexican deserts effectively separated the main native American civilizations. Although food production spread quickly from the Fertile Crescent to Ethiopia, the geographic barriers of subsaharan Africa slowed further diffusion to a crawl. To this day, tropical African crops have not been adapted to the Mediterranean conditions of South Africa's Cape Province.³

¹ Jeffrey Sachs, "Notes on a New Sociology of Economic Development," in Lawrence E. Harrison and Samuel P. Huntington, eds., *Matters: How Values Shape Human Progress* (Basic Books, 2000).

² Jared Diamond, *Guns, Germs, and Steel: The Fates of Human Societies* (W. W. Norton, 1999).

³ Diamond also points out the difference in availability of domesticable plants and animals. For instance, 13 of the 14 ancient animal species that were domesticated and led to significant increases in food production were confined to Eurasia. Although Diamond's thesis that accidents of nature and geography explain the different levels of development is fairly deterministic—some would say fatalistic—it nonetheless has significant value in accounting for the speed with which the various societies developed different levels of complexity.

The geographic conditions that facilitated the spread of food production in Eurasia and limited its spread in other regions have been critical to the diffusion of technology and ideas. Fernand Braudel, reflecting on the evolution of civilizations and echoing scholars since the Enlightenment, observed that “all thought draws life from contacts and exchanges.”⁴ Diamond’s and Wright’s analyses of broad historical trends demonstrate this amply, showing how technology and ideas throughout history have developed through their diffusion and how technology advances cumulatively, rather than in isolated epiphanies. Most innovations are borrowed from others (often other societies) and improved upon. Steam engines from Britain were critical to French industrialization; the French discovery that steam could move a piston was critical to the British invention of the steam engine; and financial mechanisms imported from Italy (which probably originated in Islamic civilization) lubricated both British and French capitalism. The diffusion of a technology is often more important than its invention, since most significant technological advances depend upon previous mastery of simpler problems, and/or being combined with other technological innovations. Consequently, technological development occurs most often and accelerates most rapidly where there is an existing base of technology on which to build.

These two rules—that geographic conditions are crucial to the diffusion of technology and ideas and that innovations develop through diffusion—have operated against non-Western societies that were initially disadvantaged by barriers to diffusion. At best, non-Eurasian societies have been playing catch-up with Eurasia; more often, they have been dominated economically, militarily, and culturally by the more technologically advanced societies derived from Eurasia. Those societies that have not adopted new technologies because geographic or other conditions excluded them from the interchange of ideas have suffered the consequences. This process has been repeated countless times throughout history: aborigines without iron were supplanted by iron-age Bantus in Africa and native Americans were supplanted by Europeans with guns and horses (and deadly germs). In modern times, poor countries that used to enjoy large amounts of foreign exchange from basic commodities such as copper, the production of which was once a cutting-edge technology, suffered the economic consequences when new technologies (e.g., fiber optics) they failed to adopt reduced demand for the old product.

Some societies consciously opted out of the interchange required for innovation. Local political conflicts during the Ming Dynasty in the fifteenth century led to China’s becoming isolationist. China had been an exporter of ideas and technology to the Middle East and Europe for centuries and had

⁴Fernand Braudel, *A History of Civilizations* (Allen Lane, 1987).

given birth to virtually all of the technology that led to the industrial revolution. But, due to a complex mixture of historic and cultural factors, it opted out of this interchange just as Europe was beginning to export technology and ideas for the first time.

Ottoman rulers, too, fearing corrupting cultural influences from the West, closed their society to exchange with Europe as Europe began to take off. This was one factor contributing to the decline of technological innovation in the Ottoman Empire, compared to the Middle Ages, when the Islamic civilization led the world in science, math, and technology. Islamic scholars between the ninth and eleventh centuries concluded that the answers to all important questions were already available and, thus, students needed only to learn existing knowledge. This approach to education resulted in rote learning and a culturally inward focus, which served to stifle creativity and suppress economic and technological innovation, leaving room for Europe's commerce and technology to eventually surpass that of the Islamic world.⁵ Islamic civilization's inward focus prevented the Near Eastern countries from engaging in a meaningful intellectual exploration of the transformations in Europe. Muslim scholars of the seventeenth and eighteenth centuries were aware of the decline of Islamic civilization but saw Europe's advantage as consisting essentially of superior weaponry, failing to analyze the deeper causes.⁶

Another factor in the decline of Islamic civilization was its loss of control of trade routes. Historically, the Near East's importance derived from its being an intermediary continent linking the vast regions of Europe, the Far East, and Africa. The Near Eastern empires controlled trade by land and then, as the dominant sea powers in the Mediterranean and the Indian Ocean, by sea, benefiting from the diffusion of technology and ideas that spread through trade. However, Europe's economic and technological ascendancy ultimately resulted in European dominance of the sea routes. By the thirteenth century, Europeans had achieved virtually complete control of the Mediterranean. Islamic civilization's loss of control over sea routes, combined with its decision to close itself off, led to economic and technological stagnation. As Braudel puts it, "from then onwards, Islam's flank was turned."⁷

Low-income countries continue to be relatively isolated from the intercourse that breathes life into technological innovation. Jeffrey Sachs divides countries into three categories: those that create new technology, those that adopt it, and those that are left behind. Sachs and Michael Porter

⁵ Timur Kuran, "Islam and Underdevelopment: An Old Puzzle Revisited," *Journal of Institutional and Theoretical Economics*, vol. 153 (1997).

⁶ Bernard Lewis, *Islam in History: Ideas, People, and Events in the Middle East* (Open Court, 1993).

⁷ Braudel, *A History of Civilizations*.

have argued that these divisions are critical in accounting for differences in growth.⁸ In order to grow, developing countries must adopt, borrow, and lend freely and frequently from everyone and anyone, consciously building a base for further new technologies.

Poor countries need to make vibrant interaction a high priority. Sachs has proposed a strategy for technological promotion involving government, academia, and industry in partnership with international donors to create a network of long- and short-term exchange relationships with Western think tanks, universities, and the research arms of multinational firms.⁹ With their low knowledge and technological base, many poor countries have low returns on investment in research and new technologies. In such an environment, private entrepreneurs have little incentive to invest in knowledge. Thus, some public intervention will be necessary for poor countries to promote basic research and new technologies. This can be done by fostering the linkages Sachs recommends or, as William Easterly has proposed, creating incentives through subsidies.¹⁰ Whatever form it takes, to ensure that it does not disincentivize private investment, any public intervention must be implemented transparently and equitably. Perhaps the most successful example involving such linkages was the Green Revolution, in which funding from donor nations, private foundations, and some low-income countries to a variety of agricultural research institutions spurred great increases in agricultural production in Asia in the 1960s.¹¹

Poor countries should also look for opportunities to expand regional linkages, dialogue, and trade. The more vigorous and frequent the contact with the larger number of societies, the better. Some countries will need to put aside regional animosities or competitive fears of sharing technology to realize the gains that can come from mutual collaboration. Iran and Iraq, for instance, could benefit greatly from collaborating with each other and opening up to the world, and they would also benefit from more open contact with their moderate neighbor, Turkey. Along the same lines, India and Pakistan and, to a lesser extent, Chile and Argentina would profit from reduced tension and greater collaboration. Poor countries must also harness the intellectual power of their own cities by allowing for the free flow of information and ideas. With their larger population densities, cities have historically been the prime localities for the exchange of ideas and thus often serve to facilitate technological innovation. The high-tech cluster in Silicon

⁸Jeffrey Sachs, "Sachs on Globalisation: A New Map of the World," *Economist*, June 24, 2000; Michael Porter, "Attitudes, Values, Beliefs, and the Microeconomics of Prosperity," in Harrison and Huntington, *Culture Matters*.

⁹Sachs, "Sachs on Globalisation."

¹⁰William Easterly, *The Elusive Quest for Growth: Economists' Adventures and Misadventures in the Tropics* (MIT, 2001).

¹¹Sachs, "Sachs on Globalisation."

Valley and the financial district in New York are but two examples. The success of both of these clusters involves intensive and ongoing collaboration and movement of people among the private business community, academia, and, to some extent, government.

Some countries continue to purposely restrict outside contacts and information flow, even among their own citizens, due to concern over political dissension or fear of outside corrupting influences, with North Korea and Cuba being the worst offenders. Historically, such actions have been a prescription for relative impoverishment and technological backwardness. Although Middle Eastern countries do not suffer from geographic barriers to the diffusion of ideas, many of them remain uninterested in—and some even hostile to—the types of outside exchanges that stimulate innovation. Even in a moderate country such as Egypt, one finds relatively little awareness of cultural, political, and economic developments in the West. As was the case in the Middle Ages, many Egyptians continue to focus on importing technology to solve problems: discussions of education reform frequently center on the need to import computers for schools; debates on agricultural productivity quickly focus on the need for foreign experts in genetic research; and the health care sector is often focused on obtaining funding for the purchase of advanced laboratory or treatment equipment. While poor countries certainly need these technologies, creating an environment that stimulates innovation requires much more: an openness to external exchanges, a willingness to allow for internal dialogue and debate, and the conscious nurturing of intellectual inquisitiveness and creativity.

The nations of the Far East—particularly Taiwan, Hong Kong, Singapore, and Korea—overcame their earlier cultural reluctance to engage in a wide range of cultural and economic exchanges with the outside world; this was an important factor in their unprecedented levels of economic growth. Even China, whose inward focus is legendary, has increasingly opened up to the world in the past twenty years. Political and economic leaders in poor countries, particularly Middle Eastern nations, must follow this example.

Communications: It Makes the World Go Round

The spread of communications technologies, like other technologies, is significantly influenced by geographic barriers. Because communications tools are themselves a medium for the spread of the technology and ideas, which in turn are essential to innovation and growth, they are the vital lubricant for economic development.

The use of communications tools has been critical in enabling some nations to create more complex organizations and wealthier societies. Writing was the principal tool that enabled societies to solve the trust

problem of economic transactions: the Sumerians of Mesopotamia, who first invented writing around 3000 BCE, initially used it to record business transactions and prevent cheating. Writing was initially used for the same purpose in ancient Egypt and China. Successive advances in writing (e.g., the development of the alphabet, the addition of vowels, and the invention of the printing press) made it more broadly accessible, increasing opportunities for mutually beneficial economic, technological, and idea exchange. Societies that did not use writing to solve the trust problem failed to grow.¹²

Societies that used communications tools most effectively quickly adopted technological advances and made them broadly accessible to their populations. In so doing, these societies greatly expanded opportunities for economic transactions and the further exchange of ideas and technology. Advances in communications tools lower the cost and increase the speed and number of exchanges that feed innovation. The printing press had this effect in Medieval Europe.¹³ Europe's adoption of this advance greatly increased the exchange of technology and ideas. Conversely, by banning printing due to its fear of corrupting Western influences, the Ottoman Empire hastened its own technological and economic decline.

Significant advances in communications technologies in the modern era allow for more rapid and extensive diffusion of existing technology and ideas than ever before, and they can overcome geographic barriers that have historically been impediments to such diffusion in certain parts of the world. They have vastly expanded the web of interconnectedness—for those who are “plugged in.”

Cutting-edge communications technologies allow people living in countries disadvantaged by geographic barriers to idea and technology diffusion to plug into the world's “social brain.” Realizing this potential requires, at a minimum, broad literacy, investment in communications technology, and openness to the free exchange of ideas. The paradox is that the countries least able to afford the technologies are the ones in the greatest need of taking advantage of them to overcome geographic barriers.

Thomas Friedman measures countries' degree of “connectivity”—how broadly countries have linked computers together into networks within

¹² Robert Wright, *Nonzero: The Logic of Human Destiny* (Pantheon, 2000). Wright applies non-zero sum game theory to explain the development of increasingly complex societies. He argues that unconsciously, societies became increasingly complex over time—i.e., embedded in larger and richer webs of interdependence—by seeking to take advantage of areas of overlapping interests. Like Diamond's, Wright's work offers useful insights into the evolution of human societies, but is ultimately overly determinist. Viewing history solely through the lens of non-zero sum game theory would lead one to conclude that the arrow of human history will lead inexorably to a peaceful, unified world government, which is difficult to envision given the myriad other factors (e.g., religion, language, culture, and trade) that continue to divide humanity and perpetuate conflict.

¹³ Wright, *Nonzero*.

and among companies, schools, and other institutions, and then linked these intranets to the Internet—in bandwidth: the capacity of the telecommunications infrastructure to carry communications. Friedman's degree of connectivity is a good predictor of a society's level of future innovation. Jobs, knowledge, and economic growth will gravitate to those countries that are the most connected.¹⁴ This is especially true for countries that are structurally open to new people and ideas through liberal immigration, publication, and trade regimes. With the open trade, investment, and financial systems of the twenty-first century, this will happen more quickly than ever before. The economic and technological decline of the Ottoman Empire took from the fifteenth through the nineteenth centuries. Economic and technological regression in today's high-tech world could occur in less than a decade. Although the Internet is worldwide, low-income countries, not surprisingly, are significantly less connected than wealthy nations. African countries, particularly the land-locked ones, have the lowest degree of connectivity.

Poor countries need to access today's communications technologies to plug into the world's social brain. Donors have expanded access to writing in low-income countries by improving literacy rates. While this remains an important foundation of development programs, donors and host countries must make the Internet more broadly available to citizens in poor countries. Some countries must put aside fears of opening up their systems and actively encourage intranets within government, academic, and private organizations. They must make the infrastructure of communications technology more affordable by lowering, and eventually eliminating, tariffs on computer hardware and software. They must make investments in computer resources for schools and provide adequate bandwidth. A number of low-income countries have recognized the importance of the Internet and have already taken some of these steps. For African countries with the least resources but the greatest need for these technologies, donors must continue to provide assistance.

Being "wired" alone is not enough to bring poor countries up to the West's level of technological innovation. Because low-income countries do not have an existing broad base of technological knowledge on which to build, other catalysts are also required.

¹⁴Thomas L. Friedman, *The Lexus and the Olive Tree* (Farrar Straus & Giroux, 1999). Friedman engagingly describes the irresistible onslaught of globalization as the integration of markets, nation-states, and technology, which has enabled individuals, corporations, and nations to reach around the world farther, faster, and deeper than ever before. Innovations in communications, computerization, miniaturization, and digitization have so lowered the cost of communications that the technology is more broadly available than ever before. Friedman views this as a recent occurrence rather than the culmination of a long-developing process. Given the pivotal role of communications technologies to wealth creation and technological advancement going back to ancient times, however, the twentieth-century information revolution cannot really be described as completely new, even if its magnitude is unequalled.

Decentralization: Let a Thousand Flowers Bloom

The decentralized competitive environment of Medieval Europe stimulated technological and idea development and helped bring about the rise of capitalism and the industrial revolution. By contrast, the more technologically advanced empires of China and the Near East began to stagnate in the Middle Ages. One key reason for their decline is that their centralized systems stifled innovation.

China made a number of isolationist decisions in the late fourteenth and early fifteenth centuries,¹⁵ leading it to abandon shipbuilding, exploration, and various mechanical technologies. Local political factors were the proximate cause of China's isolationist policies, but it was its centralized system that allowed these policies to be implemented over its vast landscape. China has essentially remained politically unified since 221 BCE. It has a relatively smooth coastline, is bound by two navigable rivers, and does not have significant mountain barriers. These geographic factors facilitated its political, military, cultural, and economic unity.

Europe has never been unified. The closest it ever came to unification was under the Roman Empire, which never controlled more than half of Europe's area. Even this limited amount of central rule over Europe ended in the fifth century CE, with the barbarian destruction of the western Roman Empire. Europe became a collection of principalities under feudalism: there were some thousand of these in the fourteenth century. Today, Western Europe comprises some forty states. Europe's highly indented coastline, formidable mountains, and lack of rivers to connect the continent have prevented determined men like Charlemagne, Napoleon, and Hitler from uniting it.

The differing effects of China's unity and Europe's disunity on innovation and growth have been remarkable. China's unity gave it an initial advantage over Europe in terms of technology and idea diffusion. Once development in the resource-rich climate of Europe got off the ground, however, its decentralized environment stimulated continuing innovation. Europe's geographic barriers were formidable enough to prevent political unification but not technological diffusion. The competitive environment this created meant that a principality that did not pursue or adopt an innovation would be left behind economically. In Europe, numerous ideas that were initially rejected were eventually adopted, copied, improved upon, and spread, including firearms, electric lighting, and printing. In China, political unification allowed centrally made poor decisions to be implemented over a wide area. Europeans did make self-defeating decisions, but these had a different effect in its decentralized environment than they would have had in China. Some other neighboring prince or king ultimately tried a better policy

¹⁵ Diamond, *Guns, Germs and Steel* (1999); Wright, *Nonzero*.

or adopted a rejected technology. Ideas spread so fast that patent rights were developed in Venice in 1474 and spread to much of Europe in less than one hundred years.¹⁶

The rise of capitalism in Europe is particularly instructive regarding the effects of decentralization on innovation. Although both Islamic and Chinese civilizations began using financial instruments to pool capital for trade in the Middle Ages, it was in northern Italy that real experimentation with financial instruments took off. In the tenth century, perhaps borrowing from Islamic civilization, northern Italians began using the *contratto di commenda*, which allowed large and small investors to underwrite a ship's trading expedition. By the fourteenth century, Venetian bankers realized they could lend out a fraction of their deposits, since all depositors were unlikely to withdraw their cash at once. (Of course, when a wide-scale lack of confidence arises and depositors attempt to withdraw all their funds, a broad economic depression can result, as in 1929. In modern times, the interconnections of the world financial systems mean that recessions or financial meltdown in one region can have severe adverse financial impacts globally, as happened with Southeast Asia's financial shocks in the late 1990s.) These mechanisms of capital formation had an empowering effect because decisions regarding the allocation of financial resources were made by diverse investors, not by the central government. In a virtuous cycle, this diffusion of economic decision-making operated to stimulate innovation even further.¹⁷

Developments in medieval England also highlight the importance of a decentralized environment. Medieval English kings had limited success in extending their administrative and legal control throughout their territories, in contrast to China and Russia at the time. This decentralization was key to the growth of trading towns and the beginnings of strong commercial impulses in medieval English society—the society that launched the industrial revolution. As exports of wool became more lucrative, creative members of the landed aristocracy realized they could make more money by evicting their feudal tenants (peasants) and renting out the land for sheep farming. The decentralized English system allowed this to happen and resulted in many copycats among feudal lords and the wealthier peasants. They eventually realized that other forms of commercial agriculture, in addition to sheep farming, could also be lucrative. The rise of commercial agriculture in England slowly changed cultural attitudes about land. It was no longer something that organized social relations between lord and peasant, but instead was increasingly perceived as investment capital that could be bought and sold.¹⁸

¹⁶ Ibid.

¹⁷ Wright, *Nonzero*.

¹⁸ Barrington Moore, *The Social Origins of Dictatorship and Democracy: Lord and Peasant in the Making of the Modern World* (Beacon Press, 1966).

As decentralization stimulated innovation in medieval Europe, it also empowered the merchant class. The broader allocation of capital, spurred by decentralization, distributed economic power more broadly across European societies. The empowered merchants pushed for policy changes, including more decentralization. They sensed their common interests and united together to demand a range of freedoms: from excessive taxation; to buy and sell property; and to enter into and enforce contracts. They ensured that the legislative and policy environment facilitated business. The great royal powers of Europe, on the other hand, spent much of the late Middle Ages preoccupied with military adventure, including religious wars.¹⁹

To be sure, many factors contributed to the rise of capitalism and the industrial revolution in Europe. Agricultural surpluses created by technological advances in farming and enrichment from the New World colonies provided the necessary capital, for instance. But Europe's decentralized environment was a critical factor in its pulling ahead of other regions.

Recent events in China also highlight the importance of decentralization. China experienced annual growth rates averaging 10 percent during the 1980s and 1990s, following its substantial decentralization of economic decision-making to the provinces. Since 1978, China has largely abandoned central planning and reduced by almost two-thirds the number of posts of governor and mayor controlled by central government.

The United States, the largest and most vibrant and innovative economy ever, institutionalized a decentralized, "federalist" system in its constitution. The large degree of autonomy granted to the states in the U.S. created an environment of cooperative competition that has fueled innovation for more than two centuries.

For low-income countries today, these historical trends show that a competitive decentralized system, operating within an environment that promotes the exchange of ideas and technology, is essential to stimulating innovation and generating growth. Poor countries must grant more autonomy to their provinces and allow for experimentation. Most Near Eastern and African countries have highly centralized systems of government. Egypt, which probably invented centralized bureaucracy in Pharaonic times, remains largely centralized today, having failed to adopt the more efficient decentralized forms of organization to which other countries turned. When

¹⁹Wright, *Nonzero*. In analyzing the state's role in economic growth in medieval Europe, Bradford De Long explains that those areas of Europe in 1500 that were the richest and most technologically advanced—the cities of northern Italy and the southern Netherlands—were the ones that had gained the largest degree of independence from centralized political control. Southern Italy was quite advanced in the year 1000, but, by 1500 had become an economic backwater compared to the north after five centuries of central absolutist rule from Sicily. J. Bradford De Long, "Overstrong Against Thyself: War, the State, and Growth in Europe on the Eve of the Industrial Revolution," in Mancur Olson and Satu Kahkonen, eds., *A Not-So-Dismal Science: A Broader View of Economies and Societies* (Oxford, 2000).

centralized governments, such as those in Africa or the Near East, do decide to start new programs to address development challenges, their inclination is to implement them through an inefficient centralized bureaucracy. South Africa, like China, has recently made tremendous strides in decentralizing its system of governance, in exception to this general pattern, and its lead must be followed.

Many donors have funded democracy and governance programs promoting decentralization. After years of piloting these programs, however, it is important for low-income nations to move toward the level of decentralized political and economic decision-making that created such unprecedented innovation in Europe and the United States. Decentralized decision-making will allow for flexibility and stimulate innovation: different regions within countries will be able to adjust to world trends without waiting for the central government to recognize what is happening and decide how to respond.

As low-income countries decentralize, they will need to determine, first, the appropriate level to which they should devolve responsibility for different functions and, second, an equitable means of financing local authorities, through such mechanisms as intergovernmental transfers and/or local taxation. Finally, they will have to put in place some form of regulatory system that establishes relationships between central government and various levels of local authorities. Again, South Africa has been a leader in addressing these issues in a thorough and thoughtful manner that should generate experimentation.

Centralized authority over certain functions is necessary for countries to take advantage of the efficiencies created by economies of scale. The precise extent of centralized authority, however, is something that should be a topic for vigorous debate. In many ways, U.S. history can be seen as one long dialogue about federal versus state rights. Active debate on these issues continues in the United States; the authorities and roles that are considered appropriate for the federal versus state governments (and the private sector for that matter) evolve over time. This is particularly true as new issues and concerns emerge on the national stage: e.g., educational policy/school desegregation, water management, worker safety, telecommunications regulation, and environmental policy. The fact that the debate continues in and of itself helps to stimulate innovation in the United States. Poor countries must allow for such dialogue and remain open and flexible to adjustments over time.

As stated earlier, in medieval Europe the rising merchant class pushed for the policy reforms that fostered business growth, and this is important. Many donors promote government-run economic policy reform programs as the essential ingredient for sustained growth: get the macroeconomic policies right and investment and increased growth will follow. One cannot dispute the value of a policy environment conducive to economic growth and investment. At the same time, there are many factors other than the macroeconomic policy

environment that impede growth. In the modern world of intense competition for foreign direct investment (FDI), geographic, health, environmental and governance issues, among others, play an important role. Good policies alone will not overcome these problems and create growth. Investors, both domestic and international, often want concrete examples of success, rather than relying on ministerial pronouncements from a centralized government. Moreover, policy reforms that impose fiscal discipline on poor countries can come at the expense of popular support. This is typically because the populace experiences the austerity consequences in the short term, whereas the economic payoff of increased growth can be years out into the future.

One way out of this dilemma is for low-income countries to create success stories by aggressively promoting business growth, which in turn will further policy reform. They must make investment capital broadly available to fuel growth and thereby create jobs. Many donors and poor countries have promoted small business lending programs. Such programs are important for making financing available to the poor, but in many cases pilot programs still need to be brought to scale. Moreover, increasing productivity in the modern world depends on the microeconomics of developing a competitive advantage in particular industries or sectors. Such a competitive advantage can be achieved by using various strategies, such as customer segmentation, differentiated products and services, strategic partnerships and appropriate technology.²⁰

Low-income countries must also take part in what Thomas Friedman has called the “democratization of finance” by using new financial mechanisms and technologies that broaden access to investment capital.²¹ Since the 1980s, debt securitization, mutual funds, and venture capital firms have made it easier than ever before for individuals and small firms to obtain equity and debt capital. Combined with advances in information technology, these financial mechanisms coalesced in the 1990s. The United States, which took more advantage of these new financial ideas, products, and services than any other country and made them more broadly available than anyone else, experienced exceptional growth. The United States averaged annual growth of 3.5 percent during the entire decade of the 1990s. With the exceptions of Norway and Australia, this significantly exceeded the growth of all other industrial countries. Germany, France, and Japan, by comparison, averaged annual growth during the 1990s of 1.5, 1.7, and 1.3 percent, respectively.²²

Of course, poor nations should not abandon macroeconomic policy reform programs. Consistently implemented, such programs send important signals to domestic and international investors about a country’s climate for

²⁰ Michael Porter, “Attitudes, Values, Beliefs, and the Microeconomics of Prosperity,” in Harrison and Huntington, *Culture Matters*.

²¹ Friedman, *The Lexus and the Olive Tree*.

²² World Bank’s 2002 World Development Indicators Report.

investment. An essential part of such macroeconomic reform programs is getting the government out of the productive sectors of the economy—i.e., privatizing state-owned enterprises—to eliminate inefficiencies and open up opportunities for private entrepreneurship. It is also important to eliminate the mass of overlapping and confusing rules and registration requirements that exist in the centralized bureaucracies found in many low-income countries. These rules prevent economic growth and restrict opportunities for the poor and middle class.²³ In some countries, small businesses must complete dozens of steps in order to register legally. For countries seeking to increase incomes for the poor, it's nonsensical to erect such barriers to entrepreneurship. It is obviously important for countries to chip away at such restrictive and illogical requirements, but working through a centralized system to chip away at the effects of centralized control will not be sufficient to realize growth. Aggressively promoting decentralization, experimentation, and business growth will, as in medieval Europe, create a constituency that will push for reforms of bureaucratic rules. Accordingly, parallel with macroeconomic reform efforts, poor countries and donors must build business success stories that create jobs and wealth and expand the constituency for reform.

Some countries fear the consequences of decentralizing and empowering the business class.²⁴ The UN *2002 Human Development Report* focuses on the symbiotic relationship between democratic governance and economic development. Medieval European burghers, after pushing for economic reforms, ultimately sought and gained the freedom of self-government—at least for merchants. Political power was indeed closely linked with the expansion of economic power in medieval Europe, and the process was not always peaceful. Nonetheless, low-income countries must overcome these fears about decentralizing economic power if they are to escape relative impoverishment.

Cultural Obstacles to Development and the Need for Visionary Leadership

Cultural factors can also present a significant obstacle to economic development. Because cultural practices and beliefs are deeply embedded and involve issues of national identity, addressing these cultural barriers requires low-income countries to cultivate visionary, home-grown leaders.

Scholars who view cultural factors as the primary determinant of the different levels of economic growth among nations often point to the West's culture, spurred by the Protestant Reformation, of scientific inquiry and

²³ Hernando De Soto, *The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else* (Basic Books, 2000).

²⁴ Wright, *Nonzero*; De Long, "Overstrong Against Thyself."

entrepreneurship. Max Weber was an early proponent of this view. *Culture Matters* (2000), edited by Lawrence E. Harrison and Samuel P. Huntington, brings together a number of adherents to this perspective. These views have gained currency in the post-9/11/01 world. Cultural practices by their nature become fixed. Even when they develop for useful reasons, they tend to persist beyond the period of their usefulness. Cultural attitudes that arose as part of communal life continue into today's era of global competitiveness, even though they put societies at a disadvantage.

The culture of scientific inquiry and entrepreneurship is not the only underlying difference between rich and poor nations. There are three more fundamental cultural factors at work. First, many people in poor countries still view life as a zero-sum game. They think, or at least they act, as if there is a limited pie of resources and any attempts to expand resources for others will result in a smaller share of the pie for them. Although industrialization has shown dramatically that increased productivity can increase the pie for everyone, many countries and people have not made this mental shift. The civil war in Angola that came to an end only this past year, where the government controlled the petroleum resources and the rebels controlled the diamond wealth, is an extreme case. People trapped in the cultural perspective of life as a zero-sum game have not learned the lesson that exploiting areas of overlapping interests expands the pie for everyone.

Second, one of the most significant mental shifts of the modern era is a willingness to rethink and reexamine political, economic, and cultural practices and beliefs themselves. The accelerated pace of social and economic advances that capitalism and industrialization brought to the West was culturally destabilizing in many ways. Eventually, however, change itself has largely become accepted in the West as part of the natural order of things. Today, virtually everything is a legitimate subject for debate in the West. This willingness to reconsider everything facilitates the generation and acceptance of new ideas. In many poor countries with persistent traditional and communal attitudes, people are less willing to discuss the utility of practices, beliefs, and habits. These are often viewed with pride as part of the national culture.

Third, many countries still retain stratified social structures that resist change, rigid class or caste systems. Such rigidity impedes social mobility, which has been an important part of the economic flexibility that fueled growth in the United States. The colonial legacy of stratified societies exacerbates this problem. In many countries, people from the lower classes who attain high levels of educational success often are unable to translate this into professional and social success. Perhaps the most notorious example is India, but it is also found in regions as culturally varied as the Middle East and Latin America. Such culturally rigid social structures artificially narrow the pool of people to serve in public and private institutions, unnecessarily restricting opportunities for talented people to contribute to their country's national development.

This is not to say that low-income countries must adopt Western culture whole cloth, including the excessively materialistic aspects of American culture presented in the media to which many of them react negatively, or that all countries must move towards a homogenous culture. Cultural differences are, after all, an essential part of what provides vibrancy to the exchanges that stimulate innovation and ideas. Nonetheless, cultural attitudes that view life as a zero-sum game, that discourage the reexamination of practices and beliefs, and that rigidly stratify societies significantly impede economic growth.

Conclusion

The job ahead is admittedly difficult for low-income nations and their donors. Overcoming historical, geographic, technological, and cultural obstacles to development requires poor countries to open their societies up to interactions with the rest of the world; access cutting-edge communications technologies and provide the means to ensure that they are broadly available to their citizens; establish a competitive, decentralized environment; institute macroeconomic policy reforms; actively promote business development; and, above all, remain open to change. This is a long list of goals for many countries to achieve.

Making significant changes can be frightening, difficult, and wrenching. Donor agencies often fail to recognize the enormity of the task for their host country partners, and change often goes against the vested interests of powerful groups in a society. Genuine, long-lasting change, therefore, cannot be imposed on a society from outside, but requires domestic champions. It must come from within and be advanced by homegrown leaders with a vision of how to transform their nations into innovative, flexible, competitive societies.

Western nations had strong leaders at critical times that brought their countries together with a common vision. Jefferson, for instance, had a broad vision of the United States' spanning the continent and trading with China; Lincoln's vision maintained national unity in the face of tremendous calamity and conflict; and Garibaldi united Italy, enabling it to compete more effectively against neighboring states. These leaders, however, operated in a less competitive environment than exists today, and within societies that were already progressing culturally. It is much more difficult for poor countries to compete today than it was for European nations when they began to take off in the Middle Ages. As wealthy nations continue to propel themselves forward, the environment is ever more competitive for poor countries.

To identify visionary leaders, poor countries must aggressively institute more meritocratic systems, making educational and employment opportunities available based on potential, not status. Government, academic, and business

institutions must establish leadership training programs at various levels. Many low-income countries provide leadership training for military officers but fail to do this in any coordinated and sustained fashion for civilian leaders. Similarly, there are few business leadership training options in most poor countries. Establishing such opportunities will unleash the intellectual and creative energies of the developing world's people. It will help cultivate a cadre of leaders who will possess the vision to lead the political and business institutions of their societies into the twenty-first century.

