

There is no formula for making a country prosperous

NZZ Interview with Nobel laureate
Esther Duflo

Nobel Opinion with Nobel laureate Esther Duflo, Abdul Latif Jameel Professor of Poverty
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Abstract

Nobel laureate Esther Duflo is skeptical about single, decisive measures. She has used field trials in developing countries to study how to reduce poverty. Her research has improved the lives of 540 million people. On June 20, 2022, Nobel laureate Esther Duflo and her husband Nobel laureate Abhijit Banerjee presented their book *Good Economics for Hard Times* at a UBS Center Opinions event in Zurich. This interview was conducted by NZZ journalists Christoph Eisenring and Thomas Fuster in the course of the event.

Christoph Eisenring and Thomas Fuster, NZZ: Ms. Duflo, you worked as an economist in Russia in the early 1990s. At that time, there was great hope that the country would soon become part of the free world. What went wrong?

Ester Duflo: I find it difficult to give an answer. But I was able to observe the economic transformation at close quarters at the time. The origin of many subsequent problems is probably voucher privatization, where citizens could buy shares in state-owned companies using coupons. It was hoped that a middle class would emerge in this way. Something else happened.

Which was?

The government lost all resources without having previous revenues from a functioning tax system. The state thus dried up – and there were neither funds to support people nor to provide basic public goods. Therefore, people who were not doing well sold their vouchers at knock-down prices, which allowed a very few people to build up huge fortunes. This experiment continues to reverberate to this day. But of course, Putin's personality also plays a role in explaining the current situation.

Is it right to completely isolate Russia politically and economically now? Or will this lead to further radicalization and thus strengthen Putin?

No one knows the answer or what the endgame will be. In retrospect, many will say that we should have done this or that. But the truth is: we are moving in the dark.

Nevertheless, decisions are necessary. For example, whether to stop importing goods that finance Russia's regime. A difficult decision because it also imposes costs on us.

No, this is not a difficult decision because the costs of the sanctions are not particularly high. Economists have calculated that the costs amount to a maximum of 2 to 3 percent of gross domestic product, even in Germany, which has been hard hit. That is less than in the pandemic. Moreover, if the West had not reacted quickly and Russia had achieved a rapid military success in Ukraine, Putin would probably soon aim at new targets in Europe. The associated costs would be far greater than 3 percent of GDP. It's like the Covid pandemic.

The pandemic has shown us that our economics are very resilient in the short term.

In what way?

Shutting down the economy to contain the pandemic was also very costly. Yet it was the right thing to do, because the human and economic consequences of doing nothing would have been much more severe. It is a similar story with the Ukraine war. The cost of the sanctions is bearable. The pandemic has shown us that our economies are very resilient in the short term.

However, the sanctions seem to have had little effect so far.

Yes, they have not proven to be sufficient. One important reason is that world markets are extremely integrated, especially for oil. Therefore, Russia is still able to sell oil to China or India, for example. This would be more difficult with natural gas. Here, the costs of an embargo would be far higher – but not only for Russia, but above all for

Germany. Nevertheless, we should extend the sanctions to natural gas.

In the wake of the pandemic, the Ukraine crisis, and the lockdowns in China, many people have become aware for the first time of how interconnected and vulnerable our economies have become. Have we overdone it with globalization? Do we need to re-localize the economy?

There is another way of looking at it: Perhaps we are not globalized enough. Because today, industries show a high regional concentration. The problem with trade is not that there is too much of it, but that certain goods are only produced in a few clusters – namely China. If a city in China then decrees a lockdown, suddenly there are no more ball bearings because all ball bearings come from that city.

It would be good if the production of goods were more evenly distributed around the world.

Why do such concentrations occur?

Because there are economies of scale when the same product is produced in the same place. The result is incredible specialization. But always looking for the cheapest product is not very farsighted. In the pandemic, for example, people realized how advantageous it is when production is regionally diversified. This does not mean that Switzerland or France should produce everything themselves. But it would be good if the production of goods were more evenly distributed around the world.

How can such diversification of global production be accomplished?

That is the problem because diversification does not come naturally. Moreover, reputation building is important in international trade. For example, even if Egypt were to start producing semiconductors tomorrow, no one would think of Egypt when ordering semiconductors. Building reputation is a long and expensive process. China's dominance in many industries exacerbates this problem. Building export capacity therefore requires the commitment of governments and international organizations.

Are you advocating an industrial policy at the global level?

Yes, in some sectors. But the support does not necessarily have to come from the state. My point is: diversification is not the natural course of things. Rather, the natural course of things leads to strong concentrations in international trade.

Does the natural course of trade also lead to growing inequality? This has been an important issue in the U.S., for example, in the course of China's integration into world trade.

It depends on the country. In the U.S., the China shock undoubtedly increased pressure on wages, primarily in those regions where the industries were in direct competition with China. Jobs in North Carolina disappeared, and the unemployed received almost no help. Economic doctrine would have expected these people to move to regions with better job prospects. But that did not happen. Contrary to external perceptions, mobility in the U.S. is extremely low. And, interestingly, it declined sharply, especially at the time of the China shock.

To cushion the consequences of these shocks, unconditional basic income has been propagated for some years now as a means of security and participation. But will this lead to people no longer working?

These effects are overestimated. In Alaska, a portion of the revenue from the Petroleum Fund is distributed annually per capita, which goes in the direction of an unconditional basic income, even if it is only about 1600 dollars per year on average. But people in Alaska don't work less because of it. However, an unconditional basic income allows people not to have to take just any job, but to take some time in their job search.

So you would recommend it?

Not for rich countries, because it would be extremely expensive to give everyone a basic income with which they can live in dignity. One would then have to save in other places, for example in education. For rich countries, targeted transfers are much better. When workers lose their jobs because of automation, for example, they need retraining.

Do people generally respond less strongly to monetary incentives than economists think?

That's the way it is; they don't just change jobs because of a higher wage, and they don't necessarily leave their place of residence because of higher taxes. Economists often have a rather narrow picture of rationality. People, on the other hand, take several dimensions into account when they form a picture of the good life.

In your presentation, you cited a survey showing that economists have a very poor reputation among the public; only politicians score worse. Why does your profession have such a bad reputation?

We're just bad PR people. But seriously, the respondents probably saw economists on TV giving their economic forecasts. But even the International Monetary Fund's predictions are lousy. But if you go to an economics department at a university, they're researching a range of exciting questions – think poverty, inequality, or development.

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You are certainly one of the innovators in the field with your controlled field experiments. However, your research is sometimes criticized for being too small-scale to advance a country.

But there is no simple formula for making a country prosperous. At most, we know what not to do. Hyperinflation certainly will not create a growth-friendly environment. But otherwise?

What about good institutions, the fight against corruption, the guarantee of property rights, the rule of law: these are elements for prosperity.

Certainly, I like all that too. But how do you get from a state where these are missing to one where they are present? Here, a multitude of small steps becomes necessary in order to get from A to B.

How many people have been reached by the Massachusetts Institute of Technology-based Field Experiment Research Institute to date?

Through all the experiments, the lives of an estimated 540 million people have improved. They have benefited from measures that our research has shown to be effective.

And is there a field experiment that you are particularly proud of?

We achieved the most with the education projects. We were able to find out why children in developing countries often

learn nothing, even though they attend school, and a lot of money is spent. It wasn't because of lazy teachers or a lack of teaching materials. Rather, teachers followed a curriculum that was not geared to the children. Often, only two children in a large class could even follow. Instead, children need to be picked up where they are and not made to learn something they are not ready for. Programs specially tailored to the students now reach many millions of children in India.

In one field experiment, even your husband, Abhijit Banerjee, was the main subject.

Yes, he has become very famous in India because of his Nobel Prize. We thus recorded a clip with him. In it, he explains that if you have Corona symptoms, you should report to a health worker. These short videos have been broadcast to millions of cell phones. Through the clips, the rate of those people who reported to a health worker with symptoms doubled compared to the control group. And it was seen that where clips with appropriate recommendations were played out, more people stayed at home and traveled less.

Source

This article was first published in the newspaper NZZ on 22 June 2022. Translated and edited for layout purposes by the UBS Center.

You can find a recording of Duflo's speech and other material on the topic on the Center's website: www.ubscenter.uzh.ch

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About the speaker



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