1

"The Most Important Economist in the World"

Jeffrey Sachs

HE IS the hero of people who campaign against world poverty. Jeffrey Sachs promises *The End of Poverty*. His best-selling treatise proclaims *How We Can Make It Happen in Our Lifetime*.

Presidents and prime ministers fete the economist who rubs shoulders with pop stars in the quest to eradicate the \$1-a-day tragedy that blights the lives of a billion people. And that's not counting the further billion on \$2-a-day, surviving at the margins of biological existence.

Professor Sachs is the man with the solutions in his portmanteau. That is why the *New York Times* dubbed him "probably the most important economist in the world",[1] an accolade that followed him on his flying missions around the world. And who can doubt the credentials of the man elevated to Special Advisor to the UN Secretary-General?

From Bolivia to Poland, from the mud huts of Malawi to the mega-cities of Asia – nowhere is beyond the reach of Jeffrey Sachs. What he doesn't know about helping people to grow out of poverty can't be worth knowing – can it? Sachs advises leaders in the neo-colonised world, guiding nations, with gusto, on how to escape the poverty traps that have defied all-powerful governments for generations.

Can it happen in our lifetime? If the secrets of balanced economic growth – in which income is allowed to trickle down to the poor – really are revealed in his lectures, delivered to star-struck audiences from Moscow to Delhi and Beijing, there would be no need for further exploration of the pervasiveness of poverty: we could leave it to Professor Sachs and the United Nations. Unfortunately, as we shall discover as we retrace his steps around the globe, Sachs is part of the problem. Today, the world is no closer to *understanding* the dynamics of poverty, let alone consigning it to history. Furthermore, we will explain how, insofar as the Sachs plan may succeed, the 21st century will witness the escalation of that brand of deep poverty that is the direct result of 'progress' in market economies.[2]

Jeffrey Sachs is not distracted by self-doubt, however. He exudes the confidence of a scholar who has command of his theory. But he also believes in taking the theory out into the real world. He acquired a taste for roaming around other people's countries, starting with Bolivia in 1985, and then jetting into Poland in 1989. We begin our story with his arrival in Russia in the summer of 1990, to give detailed briefings to Soviet planners on "the logic and key principles of market reforms".[3]

During the 1980s, Mikhail Gorbachev wanted to nudge the Soviet Union away from the clutches of centralised planning, but he failed to develop a credible strategy. Enter Jeffrey Sachs, who became advisor to the young English-speaking economists who were searching for a formula to transform the USSR from the command economy into – what?

Grigory Yavlinsky, as advisor to Gorbachev, needed guidance because, locked behind the Iron Curtain, Soviet economists had been schooled in a version of capitalism that was coloured by Marxist doctrines. Turning from state-directed production to consumer-sanctioned markets would be hazardous. The reformers needed policies informed by two considerations:

- *An acute sensitivity* to the culture and psychology of the peoples of Eastern Europe was imperative. Alien laws and institutions had to blend with their history and collective sentiments in a synthesis that would enable them to navigate to the good life beyond the Iron Curtain.
- *A profound awareness* of the shortcomings of market economics was a prerequisite. The last thing these vulnerable peoples needed was the incubation on their social soil of the kind of pathologies that cultivated poverty in the West.

Russian economists could not be expected to formulate, on their own, the laws and institutions of private enterprise. They wanted to emerge out of the near catatonic state to which civil society had been reduced by communism. Collaboration with Westerners was needed to merge the technical understanding of the inner workings of the market economy with the imagination that was needed to adapt state socialism. The privilege of undertaking this task fell to Jeffrey Sachs and several close colleagues. Armed with an introduction from philanthropist George Soros, Sachs met and worked with Yavlinsky before moving on to Yegor Gaidar, an advisor to Boris Yeltsin. Gaidar was to become Prime Minister of an independent Russia. Sachs contributed to the reform plan that shaped the first fatal days of this post-Soviet country.

Today, impoverished by the economics of the 'free market', many Russians regard themselves as victims of the plan that Jeffrey Sachs endorsed. His approach emphasised money and prices. His specialty at Harvard, where he was a professor of economics, was international finance and the macro-economics of the rich West. He now recalls:

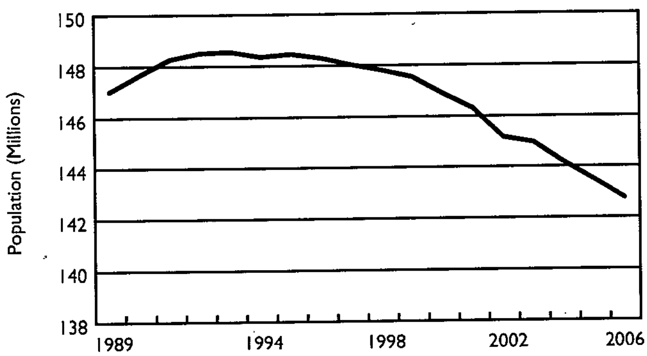
> The initial shocks of price decontrol, currency convertibility, and market liberalisation could help, as such measures did in Poland, but they would not solve the problems of underlying structural disarray, falling energy supplies, and a myriad of other interconnected crises. The reform measures, at their very best, would help to steer Russia on to a path of massive, generation-long economic and social transformation....Could it work? I thought so. I certainly thought it was worth a try.[4]

Sachs' work around the world was, by his own admission, the most challenging exercise in social engineering that could confront any economist, and yet it was approached without a first-hand understanding of "the contours of economic development and under-development in Latin America, Eastern Europe, and the former Soviet Union".[5] It was not until the early 1990s that he felt he had acquired such knowledge. And yet, he had already begun to brandish the key concepts – like *liberalisation* and *privatisation* – that the young advisors who were eager to acquire wisdom from the West would chant as magic mantras.

> My essential advice to Russia was to move quickly on the key reforms that were possible – such as stabilisation and market liberalisation – and to move definitively, although not overnight, on privatisation.[6]

Russia launched the reforms in January 1992. The plan became known as 'shock therapy'. Many people were to pay the price in the most fatal terms possible, as the graph shows.

Shock Therapy: Russia's Demographic Response



Life expectancy was reduced to the levels of the neo-colonised world. For men the average life expectancy in 1987 was 64.9 years. In 1994 this crashed to 57.5 years and in 2005 life expectancy remained below 60 years. The average life of women was also shortened, from more than 70 years (1987) to 65.3 years in 2005 – the loss of an average of five years of life. Mortality rates eclipsed the fertility of the population, which succumbed to a demographic collapse unparalleled in any European country since the days of plague. The population reached its peak of 148.6m at the end of 1993, when

Sachs ended his advisory role with the Russian government. From 1994, the shock effects of the 'therapy' administered under the tutelage of Western policy doctors saw the decimation of the population as it crashed by over 5m to 142.7m in 2006.

Sachs helped to lay the foundations for an approach to economic and social change that he carried back to New York. And there, in the corridors of the United Nations, he was given access to politicians and international civil servants who wanted to know how to eradicate poverty in the rest of the world.

UN Millennium Development Goals: Hope or Hoax?

WHILE WORKING in Moscow, Sachs proposed a transformation strategy that was composed of three main elements:

- A fund to stabilise the rouble.
- Cancellation of debts.
- Foreign aid, especially to help the most vulnerable individuals.

Sachs now points an accusing finger at financial institutions like the International Monetary Fund, and the richest nations (G7), for failing to fund his agenda. We need not doubt that his complaint has substance, that Western governments were more interested in transforming Russia into a compliant partner rather than renewing the strength of an enemy superpower.

Even so, Russia was rich in intellectual and natural resources. These could have been mobilised to facilitate her transformation, as China had done without the help of Western aid. So why did Russia fail? It failed because the Sachs model of economic development and the strategy for poverty alleviation were fatally flawed. Russia's endowment of talent was not harnessed to transform the nation. The Sachs emphasis on high finance as the cutting edge of change could not nourish the consensus that was needed to support the new institutions and bewildering practices that Russians were offered by President Yeltsin.

The crude monetarist model that was emphasised in Moscow in 1991 and 1992 could not lead the way to balanced transformation of the command economy, even if the international financiers had been generous with aid.[7] This proposition will be tested further as we explore the awesome challenges confronting poverty-stricken regions of Africa, Asia and South America. We will carry with us some of the memories of the turning points in Russia. Sachs spotlighted one of them: the Russian people fell foul of the failure of their state to protect them and the natural assets that could guarantee a flow of income into the public purse in perpetuity. The resource rents – the value of the gifts of nature – were available from the international markets to fund the restructuring of their economy and civil society. But during the two years 1995 and 1996, Sachs noted,

> Russian privatisation became a shameless and criminal activity. Essentially, a corrupt group of so-called businessmen, who later became known collectively as Russia's new oligarchs, were able to get their hands on tens of billions of dollars of natural resource wealth, mainly the oil and gas holdings of the Russian state. The

> best estimates are that about $100 billion of oil, gas, and other valuable commodities were transferred to private hands in return for perhaps no more than $1 billion of privatization receipts taken in by the Treasury.[8]

The important point for us, in considering strategies for addressing poverty, is that there was nothing in the advice offered by Sachs which, in principle, *could* have prevented the sacking of Russia's riches. Provision needed to be made, philosophically, psychologically and constitutionally, to preserve the natural resources as the fund from which the people could draw to finance the new course on which they had embarked. No such provision was made in Sachs' plan for integrating Russia into the market economy. So even if the rouble had been stabilised, debts cancelled and aid had flowed in to help pensioners, the absence of the appropriate fiscal policy meant that the state would have been vulnerable to the plunder that did, indeed, ensue.[9]

With hindsight, would Sachs have offered a different plan of campaign for Russia? We are, after all, entitled to learn from experience. Ten years later – now celebrated as "probably the most important economist in the world" – would he have modified his advice? Learning from the past was vital, for during the intervening decade his brief was extended to encompass most of the rest of the world. He roamed through the academic auditoriums and the political corridors of power in India and China and – the greatest accolade imaginable – he was mandated by the United Nations. With the prestige and power of the UN behind him, surely he would be able to succeed where sovereign governments had failed? Much depended, of course, on how the nature of poverty was characterised, if more than a televised band aid was to be applied.

To achieve the UN Millennium Development Goal of redeeming humanity by abolishing the $1-a-day syndrome, Sachs set to work by combining the scientific resources of Columbia University's Earth Institute, which he directed, with the practical knowledge of UN teams scattered around the world. Would Sachs' advice help governments to achieve sustainable growth? Would he have prescribed alternative policies if he had re-lived his three years in Moscow? We are left in no doubt: "To a large extent, the answer is no."[10]

As the Director of the UN's Millennium Project, Sachs exercised extraordinary influence. But debt cancellation and foreign aid could not be any more successful than what happened in Russia, where the people were excluded from their equal share of the oil and gas rents that the oligarchs now use to buy football clubs and real estate in the West. At the heart of the problem of poverty is a reality that was not acknowledged by Sachs, his co-workers or the international agencies that deploy massive financial power and material resources in their attacks on poverty. *Under the policies that determine the distribution of income in the capitalist economy, poverty is an institutionalised by-product of economic growth.* We shall see that growth-oriented investment retards people's development, if it is not combined with changes to the tax laws that determine the primary distribution of income.

India: Progress with Poverty

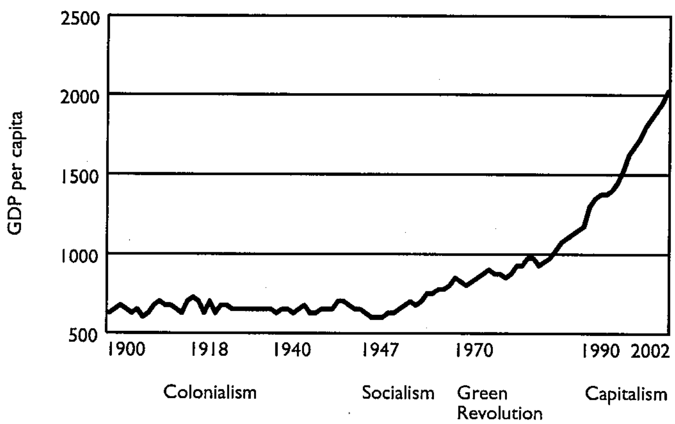
IN ASSESSING the conditions that create poverty today, it is imperative that we do not forget the influence of the past.

Disentangling the present from the influences inherited from those who lived long ago is daunting; but it has been achieved for India in a remarkable piece of research by two students of that country's colonial legacy. Their method for excavating the impact of the past on the present exposes how the practices and institutions of sovereign nations are continuing the exploitation that was supposed to be terminated by independence.

The British East India Company arrived in 1613 to launch the exploitation of the sub-continent for resources to fund first the opulent lifestyles of the aristocracy and then the industrialisation of the British economy.

With independence in 1947, India's leaders opted for socialism and centrally directed 5-Year Plans. The figure below reveals the outcome: the prosperity that the people of a post-colonial nation expected did not materialise. Under socialism, growth did not eradicate poverty, which remained the norm.

Historic Growth of the Indian Economy



Sources: Maddison (1995) and Sachs (2005) p. 181

Then, in 1970, came the Green Revolution. The West promoted a poverty-eliminating strategy based on increasing the food yields of peasants in the countryside. This did raise the profits of foreign corporations that held the patents on genetically engineered seeds and the pesticides which, for the peasants, were an expensive addition to the cost of producing food. Finally, in 1991, India turned from socialism to capitalism. Market reforms were adopted and India joined the other former socialist countries to expand and integrate the global market.

Independence did not deliver universal prosperity because India continued to live under the legacy of her former colonial masters. But how do we measure the impact of that past? Those two students of India's colonial legacy, Abhijit Banerjee and Lakshmi Iyer – economists at the Massachusetts Institute of Technology – employed advanced statistical tools. They identified the role of the British in exacerbating an already skewed distribution of wealth by creating the legal framework that continues to prejudice people's life chances today.

Given the post-independence poverty levels, they asked, how could the marked differences in income distribution, welfare and public investment within India be explained? They divided the sub-continent's regions into three categories, according to the method instituted by the British to extract rents between the 18th and 20th centuries. The table over shows the regions.

Land Tax-paying Regions, India (1757-1947)		
Zamindari (landlords)	*Raiyatwari (cultivators)*	*Mahalwari (villages)*
Bengal Bihar Orissa Tamil Nadu Andhra Pradesh	Madras Bombay Assam	North-West Provinces Panjab

The 'landlord' regions came into existence because the British misread tribal customs and turned chiefs into landowners for their revenue-collecting convenience. But in the regions where the British collected rents direct from the cultivators, they consolidated the tenure rights of the peasants. For some regions, however, they respected common ownership rights by levying rents on villages as a whole, leaving the villagers to determine how much each of them would pay.

Significantly, the soils of the landlord regions were more fertile compared with areas farmed under the other two rent-revenue models. This ought to have meant that the cultivators in these regions would prosper relative to the others. That is not what happened. For the British re-invested more of the rents in the infrastructure of the areas from which they collected revenue directly from the cultivators. The outcome, a century or more later, was clearly traceable in the levels of investment and in yields. The differences were to exercise profound consequences in the late 20th century. Some of these are summarised in the table opposite.

Inequality in 1885 was lower in those districts where the British collected rents direct from cultivators than in the landlord districts. And canal construction was funded by the

British almost exclusively in the non-landlord areas. Looking at modern-day India, Banerjee and Iyer note: "The effects we document are surprisingly large, given that we are looking at an institution that no longer exists".

The British Legacy in Post-Colonial India	
Categories	*Cultivator & Village indices compared with Landlord regions*
Irrigation	25% higher
Fertiliser use	45% higher
High-yielding rice varieties	25% higher
Agricultural productivity	16% higher, overall *with crop yields:* Rice: 17% higher Wheat: 23% higher*
Village schools availability	20-60% higher
Literacy rates	18% higher
Infant mortality	40% lower

Source: Banerjee and Iyer (2005)

* Estimates for differences in yields took into account geographic variables and the duration of British rule.

The lessons are many and varied, but we need to focus on the issues that help us to understand the causes of poverty today.

First, the British were not in India on a benevolent mission. Why, then (for example) would they invest in local irrigation networks? The answer: self-interest. In 1841, the land tax yielded 60% of total British government revenue extracted out of the sub-continent. So investing in the infrastructure increased the rental yields. The returns were not as buoyant from the landlord districts, however, because the rent collectors (the landlords) pocketed as much of the rents as they could for themselves. So fertile high-yielding regions generated lower revenues, per acre, for the British, than the marginal soils from which rents were tapped direct from cultivators and the village commons. Consequently, the British concentrated on improving the irrigation networks of the poor soils from which they could extract a higher proportion of the rents for Britain.

The landlords, on the other hand, grew richer as they privatised a growing proportion of the rents during the 19th century. And they had no legal obligation or economic incentive to reinvest in the welfare of their tenants.

> This meant that the colonial state had more at stake in the economic prosperity of non-landlord areas, since this could be translated into higher rents. This is reflected in an increasing number of legislations trying to protect the peasants from money-lenders...It also meant that the state had more reason to invest in these areas in irrigation, railways, schools and other infrastructure...[A]lmost all canals constructed by the British were in non-landlord areas. If indeed these areas had better public goods when the British left, it is plausible that they could continue to have some advantage even now.[11]

Historians have been puzzled by the large and often growing differences across the states of India, but Banerjee and Iyer have elegantly identified the core explanation. The landlord areas were drained of a larger proportion of the rents, the reciprocal of which was higher rates of illiteracy and child mortality. By not using landlords as rent-collecting intermediaries in the other regions, however, the British had greater incentive to reinvest rents in ways that would benefit the lives of those who paid the land tax direct to government.

One outcome, today, after all this time, is that non-landlord areas, in spite of their natural disadvantage, continue to outperform the landlord regions in productivity terms. Poverty reduction in modern India is higher in non-landlord areas. Scholars will continue to argue about causal mechanisms, but Banerjee and Iyer are sure of one fact.

> What seems clear is that the concentration of economic and political power in the hands of an elite, resulting from the landlord-based land tenure system, continues to be a heavy burden on the economic life of these areas.[12]

Enter Jeffrey Sachs. He arrived in 1994 – having just resigned as the Russian government's advisor – to promote his doctrine of liberalisation. His audiences were sceptical. But by the end of the century India did deliver remarkable growth rates. Did this validate the doctrine of capitalism? Sachs thought so, and he was pleased to see his proposals adopted in Delhi.

> We were delighted when the Prime Minister proclaimed [our] objectives in his message to the nation on August 15, 2000. The goal of at least 8% per year economic growth...was subsequently endorsed by India's Planning Commission.[13]

But millions of people failed to share in the good times. Why? And why did the voters eject the government in the election of 2004, "reflecting a massive vote for change emerging from India's countryside"?[14]

India was in the clutches of the growth disease – of progress associated with the poverty that was *caused* by 'progress'. This process began during the Green Revolution, which Sachs calls 'rural-led development'. Incomes were raised for a segment of the population, but this triggered a response that is part of the DNA of the modern capitalist economy. Peasants were required to pay higher rents to their landlords. If money was to be made out of the increased productivity delivered by bio-science, that money was not going to trickle down to those who toiled in the fields. Increases in the costs of fertiliser and seeds, and rents, locked the peasants in the classic trap. For many of them this had one fatal outcome: indebtedness, from which they could not escape. So began the suicides and the displacement of yet more people from the land. They had no choice but to migrate to the nearest city.[15]

The tragedy that unfolded in the countryside is told by the numbers of people seeking refuge in urban slums. The pressure was intense in Mumbai, where 60% of the population now live in slums. In the two decades of India's economic growth, the number of slum dwellers doubled, rising from 27.9m in 1981 to 61.8m in 2001 according to Kumari Selja, the Minister for Housing and Urban Poverty Alleviation.

The process of redistributing income from those who produce it to people who (as land owners) do not add value to the wealth of the nation, as illustrated by India, is inscribed into the fabric of the capitalist economy.[16] This is not a law of nature. It is sanctioned by one of two circumstances.

- **Privatisation of rental income.** This is what enriched the aristocracy in late feudal Britain, and the *zamindaris* of colonial India.
- **Redistribution by default.** If the right of producers to an equal share of the rents they produce is not protected

by law, the state's failure is exploited by opportunists. This is what enriched the oligarchs in Yeltsin's Russia.

India, as a victim of the colonial rent grab, first sought solace in socialism after independence. History has pronounced its verdict on this model. But why is the market economy also failing hundreds of millions of Indians? In 1976, the government formulated the Urban Land (Ceiling & Regulation) Act. This sought to socialise vacant land in towns to prevent the concentration of sites in the hands of profiteering speculators. Legislators realised that distortions in the market for real estate had damaging social effects. One of these was identified by Nipun Vaid in his assessment of the Act.

> Distortions in the land market often lead to land speculation which is a scenario in which the value of land is artificially raised beyond actual price and after this bubble of inflation bursts, investors in land lose out on capital as prices in the market fall.[17]

Imposing ceilings on the ownership of land, however, with the owners regulated by law and administered by civil servants, failed to deliver the benefits of an efficient property market. The Act was ordered to be deleted from the law books in 2004. The Minister of Housing and Urban Poverty Alleviation admitted that "the complexities of urban administration have grown manifold due to urban growth, population concentration, mounting poverty and unplanned spatial activities".[18]

Given such policy failures, how do we explain the extraordinary growth rates in the decade up to 2008? They were (ironically) predicated on another colonial legacy: language. The extensive use of English, combined with information technology and low wages, made it possible to service directly the needs of Western corporations.

But even as software writers prospered, their cousins in the countryside – and notably those in the regions dominated by landlords – sank deeper into debt. Someone – or something – had to be blamed. Jeffrey Sachs resorted to the device that is employed by ideologues to shut down debate about competing doctrines. He claimed that an anti-poverty 'silver bullet' did not exist. In his own words, there were "no 'magic bullets', no single solution that will put an end to global poverty".[19]

If Sachs was correct, he needed a scapegoat for poverty. He found it in resource rents. Another economist who specialised in economic development, Oxford University's Professor Paul Collier, recalled:

> Economist Jeffrey Sachs revived concern about the problem of natural resource rents. Since then political scientists have joined in, suggesting that resource revenues worsen governance.[20]

The Curse of the Resource Rents was unleashed by "the most important economist in the world". Paul Collier set out to investigate whether it was true: is nature a "curse"? Is it to blame for the blight on the lives of the billion poorest people on earth?