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## Book Review

# *Good Economics for Hard Times: Better Answers to Our Biggest Problems*

**Abhijit V. Banerjee and Esther Duflo**

Review by: Mohammad Muaz Jalil  
University of Ottawa  
mjali044@uottawa.ca

In this book<sup>1</sup>, Nobel Laureate economists Abhijit V. Banerjee and Esther Duflo cover key issues facing us, from rising inequality to migration, climate crisis, and more. The authors provide an evidence-rich, balanced, and nuanced picture of what we know: profound repercussion of “stickiness in economics”<sup>2</sup>, importance of dignity, and centrality of human well-being.

For a book with only eight substantive chapters, it includes over 650 references, drawing on cutting edge research. Each chapter typically deals with a core issue such as trade, growth, or climate, providing evidence and exploring both good and bad economics. All chapters conclude with discussions on various policy options. The authors show humility by recognizing that they may not have all the answers and with humor acknowledge that economists can often get things wrong. But they say, “there is plenty of good economics to go around” (p. 8).

The introductory chapter discusses how people have lost faith in economists; a survey in UK found that only 25% trusted economists (p. 4). Chapter 2 challenges the conventional wisdom around migration: public in developed countries overestimate the volume of immigration. It discusses that low-skill immigrants benefit local population, unlike high-skilled migrants, which is more mixed in impact. The arrival of low-skilled immigrants 1) boosts local consumption, 2) slows down mechanization, and 3) opens up new opportunity as industries relocate. The authors could have explored further the cultural dimension of anti-immigrant stances, and rise in populism<sup>3</sup>, rather than focusing mainly on traditional economics-based explanation<sup>4</sup>.

Gains from trade, examined in Chapter 3, is more ambiguous in its presentation; evidence suggests that trade liberalization may increase inequality. Path-breaking research by economist Petia Topalova showed that increased exposure to trade slowed down poverty reduction. Brand, reputation, and network often act as trade barriers. Trade is, thus, not a magic bullet, and less so for large economies because economies can be “sticky” (e.g., people are unwilling to relocate when jobs disappear) and the negative impact of trade amplifies gradually. Thus, governments need to work on redistribution and job training, and reduce relocation cost.

Chapter 4 on preference is considered by Duflo as the most important chapter and her favorite<sup>5</sup>. Here the book’s focus pivots<sup>6</sup> from neoclassical economics towards other fields, such as psychology, sociology, and behavioral economics. Contrary to economic theory<sup>7</sup>, consumers often do not know their preference and can be influenced. For example, there is an experiment showing bankers cheating when their banker identity is activated as opposed to their identity as a person belonging to a family. The chapter introduces concepts of statistical discrimination, collective action, homophily, and echo chambers, among others. It concludes by arguing that stable consistent preferences are rarely true, and interaction does not reduce prejudice, nor does confronting people with facts. Smart policies such as zoning for peace or diverting people towards policy related debate than ideological may be more helpful in changing behavior. However, the authors provide limited evidence to justify their efficacy.

Chapter 5 on growth is the most heavily cited and argues that instead of “Chasing the Growth Mirage”, we should focus on delivering well-being. Total factor productivity and spill-over from technology ideas are important but cannot fully account for growth. Efficient allocation of misallocated resources probably provides the greatest momentum, but it is limited, especially when approaching a technological frontier. The authors argue that countries

can remove egregious economic waste but should focus on improving wellbeing. They warn against industrial policies, but then do not conclude on how to remove such “egregious waste”. Furthermore, economic growth was successful in lifting over 1 billion people out of poverty<sup>8</sup>, and the number of low-income countries has halved to 34 just between 2001 and 2013<sup>9</sup>. Hence growth is still necessary and certainly not as elusive as the authors’ purport.

Chapter 6 on climate is the shortest and probably the weakest chapter. It makes a compelling case against developing countries’ complacencies towards carbon mitigation, notwithstanding the fact that developed countries are historically responsible for pollution. Technology solutions are often too optimistic; fundamentally we need to reduce our energy “addiction”. There is discussion around reframing the debate, the Green New Deal, and carbon taxation but it is not clear how to budget such programs.

Chapter 7 discusses rise of automation and high finance. Duflo and Banerjee inject a healthy dose of realism, stating that there can be too much automation; jobs in the middle may disappear, leaving us with very low-skill/high-skill jobs and inequality. Innovative solutions such as the “Robot Tax” or “Universal Basic Income (UBI)” may be difficult to implement. Unlike in Europe, the growth of high financial sectors in the United States or United Kingdom misallocated talent, and, due to a “contagion effect”, inflated CEO salaries. Evidence suggests that increased taxation reduces the use of salary as an incentive, thus reducing pre-tax inequality. Rising inequality can create social erosion, generate backlash, and rise of populism. The authors discuss these implications in the end but could have elaborated further on how inequality impacts the “common good”, eroding societal cohesion<sup>10</sup>.

Chapter 8 is an impassioned argument for state legitimacy and argues that we should limit our obsession around corruption<sup>11</sup>. Governments deal with difficult problems thus likelihood of corruption is higher. Economists have eroded people’s trust in government negatively impacting those who work there. The authors show that government-led cash transfers to the poor can do it; cash transfers can reduce inequality and the poor do not become unproductive. Furthermore, increasing taxes does not reduce work incentive. Chapter 9 is rich in policy prescriptions and supports smart social protection policies such as the Ultra UBI. They also discuss the importance of human dignity and how individuals associate their identity with work; simple income-based social protections (FLEXICURITY) are insufficient – people need respect, and to not be demonized. Transitions are costly, and economies are sticky, hence social programs should support transition: place-based economics may be sensible (e.g., EU’s agricultural policies), and subsidizing the old while facilitating youth to retrain and relocate easily. It ends with a call for action, stating “Economics is too important to be left to Economists” (p. 247).

The book has succeeded in energizing debate: left-wing economist Varoufakis finds the book’s policy prescriptions “unconvincing”, showcasing “demise of capitalism”<sup>12</sup>; at the opposite spectrum, the Wall Street Journal suggests that the prescriptions are “unconvincing” precisely because they are “ambitious” and envisages the “wholesale redesign of social programs” of our economies<sup>13</sup>. However, the book is well researched and encyclopedic, focusing on the message rather than conclusion, lucidly explaining the economic reasoning and finally, “Making Economics Great Again”, which is the title of Chapter 1.

## Endnotes

<sup>1</sup> Banerjee, A. V. & Duflo, E. (2019). *Good economics for hard times: Better answers to our biggest problems*. Penguin, UK.

<sup>2</sup> Patel, S. (2020). Book review: Good economics for hard times: better answers to our biggest problems by Abhijit V. Banerjee and Esther Duflo. *LSE Review of Books*.

<sup>3</sup> Margalit, Y. (2019). Economic insecurity and the causes of populism, reconsidered. *Journal of Economic Perspectives*, 33(4), 152-70.

<sup>4</sup> Example of Economics-based Explanation: Rodrik, D. (2017). *The economics of populism*. VOX CEPR, available at <https://voxeu.org/article/economics-populist-backlash>

<sup>5</sup> Duflo, E. (2020). *The 15<sup>th</sup> James S. Palmer Lecture Series with Professor Esther Duflo* [Video, 20-21 minute]. Retrieved from: <https://www.youtube.com/watch?v=b7tG26obvuI>

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<sup>6</sup> *ibid*

<sup>7</sup> Stigler, G. J. & Becker, G. S. (1977). De gustibus non est disputandum. *The American Economic Review*, 67(2), 76-90.

<sup>8</sup> Jean-Paul, F. & Martine, D. (Eds.). (2018). *For Good Measure Advancing Research on Well-being Metrics Beyond GDP: Advancing Research on Well-being Metrics Beyond GDP*. OECD Publishing.

<sup>9</sup> Khan, S. T. (2015, February 15). Growing up: graduation from low-income to middle-income status. *World Bank Blogs*. Retrieved from: <https://blogs.worldbank.org/developmenttalk/growing-graduation-low-income-middle-income-status>

<sup>10</sup> Sandel, M. J. (2020). *The Tyranny of Merit: What's Become of the Common Good?* London: Allen Lane.

<sup>11</sup> Duflo has made similar argument in other panel discussions. "Making Growth Work for the Poor", video of panel at World Bank-IMF Spring Meetings, April 2019; Retrieved from <https://www.youtube.com/watch?v=EEBWAGYT090&feature=youtu.be>

<sup>12</sup> Varoufakis, Y. (2019, November 11). *Good Economics for Hard Times* by Abhijit V. Banerjee and Esther Duflo review – methodical deconstruction of fake facts. *The Guardian*. Retrieved from <https://www.theguardian.com/books/2019/nov/11/good-economics-for-hard-times-abhijit-banerjee-esther-duflo-review>

<sup>13</sup> Easterly, W. (2019, November 17). Good Economics for Hard Times Review: Sticky Markets, Tricky Solutions. *The Wall Street Journal*. Retrieved from: <https://www.wsj.com/articles/good-economics-for-hard-times-review-sticky-markets-tricky-solutions-11574021736>