

The Role of Inequality and Resource Productivity for Economic Development

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Abstract

Based on fieldwork on the occupational choice and the incomes of fishermen at Chilika lagoon, India, we built an overlapping generations model of a small open economy with access to a renewable common pool resource to show how the share of the workforce in the resource sector, the average income and the income differences between the poor and the rich depend on the resource productivity and the initial distribution of wealth within the economy. A productive resource provides capital for investment in better income alternatives. The exit of individuals from the resource sector increases the income of the remaining resource harvesters. A large share of the workforce in the resource sector can overharvest the resource and impede the exit from the resource sector when they become too poor to afford the investment in income alternatives. Inequality can enhance economic development in poor resource dependent economies but reduce economic development in rich economies. Technological efficiency in resource harvesting has ambiguous impacts on economic development. This model provides an explanation why poor fishermen in developing countries can be trapped in the fishery while the fishermen in rich countries have more income options. In fact, the model can be applied in a wider context to show why some countries fail to undergo a structural transformation and remain poor with a large share of the population dependent on natural resources.