DEVELOPMENT ECONOMICS AND THE CHOICE OF DEVELOPMENT STRATEGIES

OBJECTIVE FOR TODAY
To show that to a significant extent, the choice of development strategies was supported by thinking at the time in what is now known as development economics.

WHAT IS DEVELOPMENT ECONOMICS?
This term is used to describe the strand of economics that concerns itself with the question of ‘why some countries should have developed while others remain more or less stagnant, or why some countries remain economically backward while others experience sustained secular advance’ (Leibenstein 1957).

Development economics blossomed starting from the mid 1940s, was at its strongest in the 1950s, and influenced policy most in the early 1960s. It was an off-shoot of what is sometimes referred to as structuralist economics.

Development economists were generally skeptical about the efficacy of neo-classical economics based on comparative advantage trade theory in facilitating rapid and sustained growth and also pointed out how a broadened application of the concept of external economies explained better international poverty.

While development economists differed sometimes on what caused the poverty of nations, they agreed on the following (Killick)

1. Economic development required structural transformation, (as opposed to simple economic growth);
2. Growth will only become self-sustaining after a critical or certain threshold per capita income level has been achieved; (vicious circle of poverty)
3. There was the need for a ‘critical minimum effort’ or ‘big push’ to achieve self-sustaining growth; (take-off according to Rostow, or oscillate around subsistence)
4. The most important requirement for the big push was a massive increase in the ratio of investment to income; (focusing on ICORs from the Harrod-Domar growth model)
5. Development implied industrialization, focusing on manufactures for domestic markets; (balanced versus unbalanced development argument from Hirschman who opposed agriculture)
GROWTH MODELS AND DEVELOPMENT STRATEGIES

Models can be derived from basic aggregate production functions.
\[ Y = F(K, L) \]  \hspace{1cm} (1)

Growth (from output \( Y \)) is simply a function of what happens to Capital (\( K \)) and Labour (\( L \)).

To determine how changes to capital (\( K \)) will occur it is usual to draw this from what happens to savings.

\[ S = sY \]  \hspace{1cm} (2)

Where \( S \) is total savings, \( s \) is average saving rate and \( Y \) is total income

But we know that all household current income not consumed is saved and all current production of goods not consumed currently is used for investment in closed economy, hence

\[ S = I \]  \hspace{1cm} (3)

By definition

\[ \Delta K = I \]  \hspace{1cm} (4) \hspace{0.5cm} or \hspace{0.5cm} \Delta K = I - dK \hspace{0.5cm} \text{(for depreciation)}

Combining (2) and (3)

\[ \Delta K = sY \]  \hspace{1cm} (5) \hspace{0.5cm} or \hspace{0.5cm} \Delta K = sY - dK.

This allows us to see what will motivate a change in capital stock in (1).

The **Harrod-Domar model** is derived from the production function

\[ Y = K/v \]  \hspace{1cm} (6)

Where \( v \) is a constant called the capital-output ratio. So \( v = K/Y \)

\[ \Delta Y = \Delta K/v \]  \hspace{1cm} (7)

But, by definition, the growth rate of output is simply \( \Delta Y/Y \). By dividing both sides of (7) by \( Y \) we get

\[ g = \Delta Y/Y = \Delta K/Yv \]  \hspace{1cm} (8)

And \( \Delta K = sY \). Hence if we substitute that into (8) we get

\[ g = s/v \]  \hspace{1cm} (9)
Hence growth is simply the outcome of saving and the efficiency with which capital is used in production.

**THE USE OF THE GROWTH MODELS IN PRACTICE**

Since it became obvious what will lead to growth, and what growth was desired, the only remaining thing to do was to use policy to achieve the required investments by generating the required savings (both domestic and foreign).

Planning by the state became a substitute for the market. Preparing development plans became the order of the day (Most countries had them)

There was a sense in which the theories of development were in harmony with the desires of political leaders and their ideologies.

The application of the theory suffered from many angles, including the fact that there was not an unlimited supply of capital to finance development plans built on the premises of ISI.

Despite failure and abandonment of development plans, there is still a sense that a number of the principles and the market conditions that precipitated the earlier thinking continue to be important for current thinking.