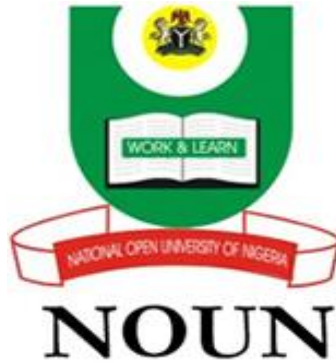

NATIONAL OPEN UNIVERSITY OF NIGERIA

DEVELOPMENT ECONOMICS

ECO 714

FACULTY OF SOCIAL SCIENCES

COURSE GUIDE

Course Developer:

Dr. Amaka G. METU

Department of Economics

Nnamdi Azikiwe University, Awka

Anambra State

Course Editor:

Professor Risikat O. S. DAUDA

Department of Economics

University of Lagos, Ojo

Lagos State

© 2020 by NOUN Press
National Open University of Nigeria,
Headquarters,
University Village,
Plot 91, Cadastral Zone,
Nnamdi Azikiwe Expressway,
Jabi, Abuja.

Lagos Office
14/16 Ahmadu Bello Way,
Victoria Island, Lagos.

e-mail: centralinfo@nou.edu.ng
URL: www.nou.edu.ng

All rights reserved. No part of this book may be reproduced, in any form or by any means, without permission in writing from the publisher. Printed: 2020

ISBN:

Printed:

ISBN:

CONTENT

Introduction

Course Content

Course Aims

Course Objectives

Working through This Course

Course Materials

Study Units

Textbooks and References

Assignment File

Presentation Schedule

Assessment

Tutor-Marked Assignment (TMAs)

Final Examination and Grading

Course Marking Scheme

Course Overview

How to Get the Most from This Course

Tutors and Tutorials

Summary

Introduction

Welcome to **ECO 714: Development Economics.**

ECO 714: DevelopmentEconomics is a two credit and one semester postgraduate course for Economics students. The course is made up of twelve units spread across fifteen lecture weeks. This course guide gives you an analytical approach to the economic problems of developing nations and efforts being made in order to breach the gap between developed and developing countries. It guides you on how to achieve the course aims and objectives successfully by adhering to the suggested general guidelines. Answers to your tutor marked assignments (TMAs) are within the material.

Course Content

This course is basically oneconomic development, as an aspiring economist, you should be able to understand the theoretical foundations of developed economies and how to adopt it in solving socioeconomic problems of developing nations. The topics covered include: meaning and measurement of economic growth and economic development, selected theories and strategies of economic growth and development as well as issues concerning sustainable development.

Course Aims

The aims of this course is to give students a comprehensive understanding as regards:

- Fundamental concepts on economic growth and economic development.
- To familiarize you on how to measure economic growth and development.
- To expose you to the differences between economic growth and economic development
- To guide you in understanding the determinants of economic development.
- To expose you on the challenges of achieving economic development.
- To stimulate you in understanding issues on sustainable development

- To acquaint you in understanding some growth and development theories/models and their policy implications.
- To guide you in understanding some economic development strategies.
- To familiarize you on the role of capital formation in economic development
- To intimate you the different economic development strategies in developing countries.
- To expose you to the role of foreign trade in developing countries.

Course Objectives

To achieve the aims of this course, there are different specific objectives which the course is out to achieve and they are set out for each unit. Each unit starts with some listed objectives and you are expected to read them before working through the unit. After completing each unit, you are to refer back to the stated objectives. The essence is to assist you in accomplishing the tasks entailed in this course and help you assess if you have done what is required from the unit. By the end of the course period, you are expected to be able to:

- Enumerate why Development Economics should be studied
- Explain the concept of economic growth
- Describe how economic growth is measured
- Illustrate the components of economic growth
- Discuss the meaning of economic development
- Enumerate the core values of economic development
- Explain how economic development is measured
- Differentiate between economic growth and development.
- Discuss the meaning of sustainable development
- Outline the pillars of sustainable development
- Highlight the goals of sustainable development
- Explain policies on sustainable development.

- Explain the Lewis development theory
- Highlight the assumptions of Lewis' model
- Give a critical evaluation of Lewis' model
- Discuss the relevance of Lewis' model to developing economies.
- Discuss the neoclassical growth model.
- Highlight the assumptions of neoclassical growth model.
- Explain the implications of neoclassical growth model to the developing countries
- Discuss the balanced growth development strategy
- Explain the unbalanced growth strategy
- Give a critical appraisal of both balancedand unbalanced growth strategies
- Explain the meaning of import substitution strategy
- Identify the advantages and disadvantages of import substitution strategy
- Discuss the meaning of export promotion strategy
- Outline the measures for export promotion strategy
- Explain the meaning of foreign trade
- Outline the role of foreign trade in economic development
- Describe the limitations of foreign trade in developing countries.

Working through the Course

To successfully complete this course, you are required to read the study units, the referenced books and other materials on the course. Each unit contains self-assessment exercises called Student Assessment Exercises (SAE), and in some cases will be required to submit assignments for assessment purposes. At the end of the course there is a final examination. This course should take about 15weeks to complete and some components of the course are outlined under the course material subsection.

Course Material

This section contains the major component of the course and time allocation for a successful and timely completion of the course unit. The list includes:

1. Course guide
2. Study unit
3. List of References
4. Assignment file
5. Presentation schedule

Study Unit

There are 12 units in this course which needs to be studied diligently and carefully so as to achieve the set objectives.

MODULE ONE: NATURE AND BASIC ECONOMIC DEVELOPMENT PROBLEMS

Unit 1 Economic Growth and Development
Unit 2 Meaning and Measurement of Economic Development
Unit 3 Development and Underdevelopment
Unit 4 Issues on Sustainable Development

MODULE TWO: SELECTED THEORIES OF ECONOMIC GROWTH AND ECONOMIC DEVELOPMENT

Unit 1 The Structural Growth Theory
Unit 2 International-Dependence Theory
Unit 3 Neoclassical Growth Model
Unit 4 Endogenous Growth Model and Policy Implications

MODULE THREE: ECONOMIC DEVELOPMENT STRATEGIES

Unit 1 Balanced and Unbalanced Growth Strategy
Unit 2 Import Substitution and Export-Led Promotion Strategy
Unit 3 Capital Formation and Economic Development
Unit 4 Foreign Trade and Economic Development

Each study unit will take at least two hours, and it includes the introduction, objectives, main content, self-assessment exercise, conclusion, summary and reference. Other areas border on the Tutor-Marked Assessment (TMA) questions. Some of the self-assessment exercise will necessitate discussion, brainstorming and argument with colleagues. You are strongly advised to do so in order to understand and get acquainted with the course and its objectives.

There are also reference materials listed for further reading so as to get additional information. Study the materials; practice the self-assessment exercises and tutor-marked assignment (TMA) questions for greater and detailed understanding of the course. All these are necessary in order to achieve the stated aim and objectives.

Textbook and References

For further reading and more detailed information about the course, the following materials are recommended:

Textbook and References

For further reading and more detailed information about the course, the following materials are recommended:

Ahuja, H. L. (1980). *Modern economics*. New Delhi: S. D. Chand.

Ahuja, H. L. (2016). *Development economics*. New Delhi: S. D. Chand.

Brodhag, C., & Taliere, S. (2006). Sustainable development strategies: Tools for policy coherence. *Natural Resources Forum*, 30, 136–145. doi:10.1111/narf.2006.30.issue-2

Daly, H. E. (1992). U.N. conferences on environment and development: retrospect on Stockholm and prospects for Rio. *Ecological Economics: the Journal of the International Society for Ecological Economics*, 5, 9–14. doi:10.1016/0921-8009(92)90018-N

Diesendorf, M. (2000). Sustainability and sustainable development. In D. Dunphy, J. Benveniste, A. Griffiths, & P. Sutton (Eds.), *Sustainability: The corporate challenge of the 21st century* (pp. 2, 19–37). Sydney: Allen & Unwin

Fashola, M. A. (2001). *Macroeconomic theory highlights and policy extensions for less-developed economies, (3rd ed).* Lagos: Concepts Publishers Ltd.

Haller, A. (2012). Concepts of economic growth and development: Challenges of crises and of knowledge. Economy Trans-disciplinary cognition, 15(1), 66-71

Heloisa, M. (2012). Measuring economic progress and well-being: How to move beyond GDP. Oxfam America Research Backgrounder series. Retrieved from http://www.oxfamamerica.org/publications/measuring-economic-progress-and-well-being-how-to-move-beyond-gdp

Hicks, N. & Streeten, P. (1979). Indicators of development: The search for a basic need yardstick. *World Development,* 7(6), 568-580. www.DOI:10.1016/0305-750X(79)90093-7

Jhingan, M. L. (2013). *The economics of development and planning,(40th ed).* India: Vrinda Publications (P) Ltd. Kuznets, S. (1973). Modern economic growth: Findings and reflections. *The American Economic Review*, 63(3).

Lanza, V. (2012). *The classical approach to capital accumulation: The classical theory of growth.*www.diva-portal.org>...pdf

Mladen, M. I. (2015). Economic growth and development. *New technologies international, 3*(1), 55-62.

Mensah, J. (2019). *Sustainable development: Meaning, history, principles, pillars, and implications for human action: Literature review.* Retrieved from https://www.tandfonline.com/doi/citedby/10.1080/23311886.2019.1653531?scroll=top&needAccess=true

Metu, A. G. (2017).Economic growth and development**.** In U. R. Ezenekwe, K. O. Obi, M. C. Uzonwanne & C. U. Kalu (Eds). *Principles of economics II.* (164 - 178). Nigeria: Djompol Printers & Publishers.

Nafziger, E. W. (2006). Economic development 4th Edition. New York: Cambridge University Press.

Olajide, O. T. (2004). *Theories of economic development and planning*. Lagos: Pumark Nigeria Ltd.

Onwuka, C. E. (2011). *Economic development monograph series 3*.Ekpoma: Pon Publishers

Todaro, M. P. & Smith, S. C. (2015). *Economic development*, *12th ed*. Boston: United States of America: Pearson Publishers.

United Nations Conference on the Human Environment. (1992). Rio Declaration on Environment and Development. Rio de Janiero, Brazil: United Nations.

www.sustainabledevelopment.org

Assignment File

The assignment files and marking scheme will be made available to you. This file presents you with details of the work you must submit to your tutor for marking. The marks you obtain from these assignments shall form part of your final mark for this course. Additional information on assignments will be found in the assignment file and later in this Course Guide in the section on assessment.

There are four assignments in this course. The four course assignments will cover:

Assignment 1 - All TMAs' question in Units 1 – 4 (Module 1)

Assignment 2 - All TMAs' question in Units 5 – 8 (Module 2)

Assignment 3 - All TMAs' question in Units 9 – 12 (Module 3)

Presentation Schedule

The presentation schedule included in the course materials gives the important dates for the completion of tutor-marking assignments and attending tutorials. You are required to submit all assignments before or on the due date. Kindly guide against falling behind in your work as this may affect your overall result.

Assessment

The course will be assessed using two formats: The tutor-marked assignments as well as a written examination. The assignments submitted to your tutor for assessment will count for 30% of your total course mark while the final written examination of three hours duration will count for the remaining 70% of your total course mark.

Tutor-Marked Assignments (TMAs)

There are three tutor-marked assignments according to each unit in this course. You will submit all the assignments. You are encouraged to work all the questions thoroughly. The TMAs constitute 30% of the total score.

Assignment questions for the units in this course are contained in the Assignment File. You will be able to complete your assignments from the information and materials contained in your set books, reading and study units. However, it is desirable that you demonstrate that you have read and researched more widely than the required minimum. You should use other references to have a broad viewpoint of the subject and also to give you a deeper understanding of the subject. When you have completed each assignment, send it, together with a TMA form, to your tutor. Make sure that each assignment reaches your tutor on or before the deadline given in the Presentation File.

Final Examination and Grading

The final examination is of three hours' duration and have a grade score of 70% of the total course grade. The examination will consist of questions which reflect the types of self-assessment practice exercises and tutor-marked problems you have previously encountered.

Revise the entire course material using the time between finishing the last unit in the module and that of sitting for the final examination. You might find it useful to review your self-assessment exercises, tutor-marked assignments and comments on them before the examination. Please note that all areas of the course will be assessed.

Course Marking Scheme

The Table presented below indicates the total marks (100%) allocation.

Assignment	**Marks**
Assignments (Best three assignments out of four that is marked)	30%
Final Examination	70%
Total	**100%**

Course Overview

The Table below indicates the units, number of weeks and assignments to be taken by you to successfully complete the course, Development Economics (ECO 714)

Units	**Title of Work**	**Week's Activities**	**Assessment (end of unit)**
	Course Guide		
MODULE1:NATURE AND BASIC ECONOMIC DEVELOPMENT PROBLEMS			
1	Economic Growth and Development	Week 1	Assignment 1
2	Meaning and Measurement of Economic Development	Week 2	Assignment 1
3	Development and Underdevelopment	Week 3	Assignment 1
4	Issues on Sustainable Development	Week 4	Assignment 1
MODULE TWO: SELECTED THEORIES OF ECONOMIC GROWTH AND ECONOMIC DEVELOPMENT			
1	The Structural-Change Growth Theory	Week 5	Assignment 2

2	International-Dependence Theories	Week 6	Assignment 2
3	Neoclassical Growth Model	Week 7	Assignment 2
4	Endogenous Growth Model and Policy Implications	Week 8	Assignment 2
MODULE 3: FACTORS OF GROWTH AND ECONOMIC DEVELOPMENT STRATEGIES			
1	Balanced and Unbalanced Growth Strategy	Week 9	Assignment 3
2	Import Substitution and Export-Led Promotion Strategy	Week 10	Assignment 3
3	Capital Formation and Economic Development.	Week 11	Assignment 3
4	Foreign Trade and Economic Development	Week 12	Assignment 3

How to get the most from this Course

In distance learning the study units replace the university lecturer. This is one of the great advantages of distance learning; you can read and work through specially designed study materials at your own pace and at a time and place that suit you best.

In the same way that a lecturer might send you some readings to do, the study units guides you on when to read your books or other materials. Think of it as reading the lecture instead of listening to a lecturer and embark on discussions with your colleagues. Similarly, just as a lecturer might give you an in-class exercise, your study units provide exercises for you to do at appropriate points.

Each of the study units follow a common format. The first item is an introduction to the subject matter of the unit and how a particular unit is integrated with the other units and the course as a whole. Next is a set of learning objectives. These objectives let you know what you should be able to do by the time you have completed the unit. Hence, use these objectives as a guide. When you have finished the unit you must go back and check

whether you have achieved the objectives. If you make a habit of doing this, you will improve your chances of passing the course and getting the best grades.

The main body of the unit guides you through the required reading from other sources. This will usually be either from your set books or from a reading section. Some units require you to undertake practical overview of historical events. You will be directed when you need to embark on discussion and guided through the tasks you must do.

The purpose of the practical overview of some certain historical economic issues are in twofold. First, it will enhance your understanding of the material in the unit. Second, it will give you practical experience and skills to evaluate economic arguments, and understand the roles of history in guiding current economic policies and debates outside your studies. In any event, most of the critical thinking skills you will develop during studying are applicable in normal working practice, so it is important that you encounter them during your studies.

Self-assessments are interspersed throughout the units, and answers are given at the end of the units. Working through these tests will help you to achieve the objectives of the unit and prepare you for the assignments and the examination. You should do each self-assessment exercises as you come to it in the study unit. Also, ensure to master some major historical dates and events during the course of studying the material.

The following is a practical strategy for working through the course. If you run into any trouble, consult your tutor. Remember that your tutor's job is to help you. When you need help, don't hesitate to call and ask your tutor to provide it.

1. Read this Course Guide thoroughly.
2. Organize a study schedule. Refer to the `Course overview' for more details. Note the time you are expected to spend on each unit and how the assignments relate to the units. Important information, e.g. details of your tutorials, and the date of the first day of the semester is available from study centre. You need to gather together all this information in one place, such as your dairy or a wall calendar.

Whatever method you choose to use, you should decide on and write in your own dates for working through each unit.

3. Once you have created your own study schedule, do everything you can to stick to it. The major reason that students fail is that they get behind with their course work. If you get into difficulties with your schedule, please let your tutor know before it is too late to help.
4. Turn to Unit 1 and read the introduction and the objectives for the unit.
5. Assemble the study materials. Information about what you need for a unit is given in the `Overview' at the beginning of each unit. You will also need both the study unit you are working on and one of your set books on your desk at the same time.
6. Work through the unit. The content of the unit itself has been arranged to provide a sequence for you to follow. As you work through the unit you will be instructed to read sections from your set books or other articles. Use the unit to guide your reading.
7. Up-to-date course information will be continuously delivered to you at the study centre.
8. Work before the relevant due date (about 4 weeks before due dates), get the Assignment File for the next required assignment. Keep in mind that you will learn a lot by doing the assignments carefully. They have been designed to help you meet the objectives of the course and, therefore, will help you pass the exam. Submit all assignments no later than the due date.
9. Review the objectives for each study unit to confirm that you have achieved them. If you feel unsure about any of the objectives, review the study material or consult your tutor.
10. When you are confident that you have achieved a unit's objectives, you can then start on the next unit. Proceed unit by unit through the course and try to pace your study so that you keep yourself on schedule.
11. When you have submitted an assignment to your tutor for marking do not wait for it return `before starting on the next units. Keep to your schedule. When the

assignment is returned, pay particular attention to your tutor's comments, both on the tutor-marked assignment form and also written on the assignment. Consult your tutor as soon as possible if you have any questions or problems.

12. After completing the last unit, review the course and prepare yourself for the final examination. Check that you have achieved the unit objectives (listed at the beginning of each unit) and the course objectives (listed in this Course Guide)

Tutors and Tutorials

There are some hours of tutorials (2-hours sessions) provided in support of this course. You will be notified of the dates, times and location of these tutorials. Together with the name and phone number of your tutor, as soon as you are allocated a tutorial group.

Your tutor will mark and comment on your assignments, keep a close watch on your progress and on any difficulties you might encounter, and provide assistance to you during the course. You must mail your tutor-marked assignments to your tutor well before the due date (at least two working days are required). They will be marked by your tutor and returned to you as soon as possible.

Do not hesitate to contact your tutor by telephone, e-mail, or discussion board if you need help. The following might be circumstances in which you would find help necessary. Contact your tutor if:

• You do not understand any part of the study units or the assigned readings

• You have difficulty with the self-assessment exercises

• You have a question or problem with an assignment, with your tutor's comments on an assignment or with the grading of an assignment.

You should try your best to attend the tutorials. This is the only chance to have face to face contact with your tutor and to ask questions which are answered instantly. You can raise any problem encountered in the course of your study. To gain the maximum benefit

from course tutorials, prepare a question list before attending them. You will learn a lot from participating in discussions actively.

Summary

The course, Economic Development (ECO 714) is about economics of developing countries whose people are faced with different economic problems such as poverty, inequality, unemployment, the environment, and deficiencies of people. The course exposes you to the nature of development and why there is need to have it as a separate course of study. You will also be introduced to the differences between developed and underdeveloped countriesand the challenges of achieving economic development. Issues on sustainable development will also be studied in this course. This course will also give an insight intothe theories of economic growth and strategies of achieving economic development. Thereafter you will be stimulated to understanding the role of capital formation and accumulation in enhancing economic development. Finally, it shall enlighten you about the role of foreign trade in accelerating economic growth and development.

However, to gain a lot from the course please try to apply anything you learn in the course to term paper writing and in other Economics courses. We wish you success with the course and hope that you will find it fascinating and handy

MODULE ONE NATURE AND BASIC ECONOMIC DEVELOPMENT PROBLEMS

Unit 1 **Economic Growth and Development**
Unit 2 **Meaning and Measurement of Economic Development**
Unit 3 **Development and Underdevelopment**
Unit 4 **Issues on Sustainable Development**

UNIT 1 ECONOMIC GROWTH AND DEVELOPMENT

CONTENTS

1.0 Introduction
2.0 Objectives
3.0 Main Content
 3.1 Nature of Development Economics
 3.2 Why Study Development Economics?
 3.3 Concept of Economic Growth
 3.4 Measurement of Economic Growth
 3.5 The Components of Economic Growth
4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References/Further Readings

1.0 INTRODUCTION

There is one central and simple question in the study of economic development; what accounts for the phenomenal disparities in global living standards? In a related vein, will developing countries eventually catch up with developed countries? These and many more questions attracted the attention of many economists such as Adam Smith, Karl Marx and Keynes, especially after the Second World War, to start devoting attention to problems of underdeveloped countries. This unit examines the nature of development economics because the principles are very necessary in understanding why so many development problems remain unsolved. We will also discuss the meaning, measurement and sources of economic growth or factors that lead to creation of greater capacities to produce and generate increasing national incomes.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- Enumerate why Development Economics should be studied
- Explain the concept of economic growth
- Describe how economic growth is measured
- Illustrate the components of economic growth
- Discuss the meaning of underdevelopment
- Explain the common characteristics of underdevelopment
- Identify the major obstacles to economic development
- Enumerate the determinants of economic development

3.0 MAIN CONTENT

3.1 The Nature of Development Economics

The study of economic development is one of the newest challenging branches of the broader discipline of economics. Albeit, it could be claimed that Adam Smith was the first development economist and his study on the *Wealth of Nations,* published in 1776 was the first treatise on economic development, the systematic study of the problem and processes of economic development in Africa, Latin America and Asia just emerged over the past six decades. We begin, therefore, by contrasting modern development economics with traditional neoclassical economics and political economy.

Traditional neoclassical economics is primarily concerned with how scarce productive resources can be efficiently and effectively allocated as well as how these resources grow over time so as to produce an ever-expanding range of goods and services. Traditional economics involves studying about an advanced capitalist world with perfect markets; consumer sovereignty; decisions made on the basis of marginal, automatic price adjustments; private-profit, and utility calculations; and equilibrium outcomes in all product and resource markets.

Political economy goes beyond traditional economics to study the social and institutional processes through which certain groups of economic and political elites influence the allocation of scarce productive resources for the benefit of the society. Political economy is concerned with the role of power in making economic decisions.

Development economics is larger in scope than the traditional neoclassical economics or even political economy. It is concerned with the economic, cultural, and political requirements for effecting rapid structural and institutional transformations of the societies so as to bring about economic progress to the largest sections of the populations. It must focus on the mechanisms that keep families, regions, and even entire nations in poverty traps, and on the most effective strategies for breaking out of these traps. Therefore, a larger government role as well as some degree of coordinated economic decision making directed towards transforming the economy are usually viewed as essential components of development economics. Also, the activities of non-governmental organizations, both at the national and international level, are also receiving increasing attention due to low functionality of both governments and markets in the developing world; so as to achieve the transformation of the economy.

Due to the heterogeneity of the developing world and the complex nature of the development process, development economics must be all-embracing, combining relevant theories from traditional economic analysis with new models and broader multidisciplinary approaches derived from studying the historical and contemporary development experience of Africa, Latin America and Asia. The theories sometimes confirm or may even challenge the traditional ways of observing the world. But in all, the ultimate purpose of development economics, is to help us understand developing economies in order to help improve the material lives of the majority of the world population.

Development Economics focuses primarily on the economic, social and institutional mechanisms that are needed to bring about rapid and large-scale improvements in the standards of living for the people in developing nations. It is concerned with the formulation of suitable policies for effective economic, social and institutional transformations of entire societies within a short while (Todaro & Smith, 2015).

SELF-ASSESSMENT EXERCISE

i. Discuss the focus of Development Economics.

3.2 Why Study Development Economics?

The problems of developing economies are diverse and unique, they may not be easily understood using traditional economic theories, rather you may have to unlearn much when studying their economies. Unlike the developed countries, developing countries frequently do not have a high level of technical knowledge and educated labour force, commercial farmers, local ownership of industry, heavy reliance on direct taxes for revenue, a large number of export commodities, and an average income substantially above subsistence, a well-developed capital market, or a high savings rate. This gives rise to the study of development economics which will help the students think *systematically* about economic problems and issues, and formulate conclusions based on relevant principles and reliable statistical information. Specifically, a course in development economics would help in a better understanding of a number of mind-blowing questions as they relate to the economics of the developing economies. According to Todaro and Smith (2015) there are about thirty such questions including:

i. What is the history of economic development?
ii. What is the meaning of economic growth and economic development?
iii. Has economic growth in the third world improved the living conditions of its poor?
iv. What are the characteristics of a developing county?
v. What are the major theories of economic development?
vi. Why is there so much poverty, inequality and unemployment in developing countries?
vii. What policies are necessary for reducing these economic problems?
viii. Why is there so much gap between the rich and the poor?
ix. Are the problems of underdevelopment internally or externally induced?

x. What is the impact of poor education and health on the prospects of development, and how should the problems be addressed?

xi. Are economic privatization and free markets really the answers to the problems of underdevelopment?

xii. What are the roles of government in achieving development in their economies?

xiii. What trade strategies should developing countries use? Should they import less or export more?

xiv. Are economic policies in developing countries sustainable over time?

These questions are only some of those to be explored. An introduction to development economics should help you gain a better understanding of a number of critical questions relating to the economics of the developing world.

SELF-ASSESSMENT EXERCISE

i. Outline the reasons for study of Development Economics as a course.

3.3 The Concept of Economic Growth.

The term economic growth has been variously defined. Nafziger (2006) explains economic growth as increases in a country's production or income per capita, while the production is usually measured by gross national product (GNP) or gross national income (GNI); they are used interchangeably to measure an economy's total output of goods and services.

According to Haller (2012) economic growth, in a narrow sense, is an increase of the national income per capita in quantitative terms with a focus on the functional relations between the endogenous variables. Then in a wider sense, it involves the increase of the GDP, GNP and NI, including the production capacity, expressed in both absolute and relative size, per capita. By this definition, it means that economic growth involves the process of increasing the sizes of national economies, the macro-economic indications, especially the GDP per capita.

Todaro and Smith (2015) defines economic growth as the steady process by which the productive capacity of the economy is increased over time to bring about rising levels of national output and income. While Mladen (2015) view economic growth as constantly increasing the volume of production or the increase in gross domestic product over a period of time, usually one year.

Economic growth is a long-term rise in the capacity to supply increasingly diverse economic goods to its population. The growing capacity is based on advancing technology as well as institutional adjustments. Economic growth occurs whenever people take resources and efficiently rearrange them in ways that make them more productive overtime (Metu et al., 2017). It is the continuous improvement in the capacity to satisfy the demand for goods and services, resulting from increased production scale, and improved productivity i.e. innovations in products and processes.

Aggregate economic growth is measured in terms of gross national product (GNP) or gross domestic product (GDP), although alternative metrics are sometimes used. In a nutshell, economic growth is an increase in the capacity of an economy to produce goods and services, compared from one period of time to another. It can be measured in nominal or real terms, the latter of which is adjusted for inflation. Economic growth can be positive, zero or negative.

Positive economic growth is recorded when the annual average rhythms of the macro-indicators are higher than the average rhythms of growth of the population.
Zero economic growth is when the annual average rhythms of growth of the macro-economic indicators, particularly GDP, are equal to those of the population growth.
Negative economic growth is when the rhythms of macro-economic indicators are less than population growth.

It is expected that when the rate of economic growth is large, there will be increase in the production of goods and services and, consequently, decrease in unemployment due to increase in the number of job opportunities created; hence, improvement in the

population's standard of life. Though this analogy does not always hold in developing countries because economic growth is a complex, long-run phenomenon, subjected to constraints such as excessive rise of population, limited resources, inadequate infrastructure, inefficient utilization of resources, excessive governmental intervention, institutional and cultural models that make the increase difficult.

SELF-ASSESSMENT EXERCISE

i. Define and explain the concept of economic growth.
ii. Differentiate positive economic growth from negative economic growth

3.4 Measurement of Economic Growth

To measure economic growth rate in a country involves summing the total number of goods and services produced within the economy in the current year and compare it with that of the previous year. But, the big question is how can these products be summed up given the fact that they come in different weights and dimensions? That is how do we then measure economic growth?

In measuring economic growth, gross domestic product (GDP) or its related indicators, such as gross national product (GNP) or gross national income (GNI) which are derived from the GDP calculation is commonly used. Gross Domestic Product (GDP) is a broad measure of aggregate economic activity which can be calculated using three different approaches. The three approaches identified by Bemanke and Abel (2005) as cited in Heloisa (2012) are: The product approach, the expenditure approach, and the income approach.

- ***The product approach*** measures GDP by aggregating the market values of final goods and services that are newly produced within a nation during a fixed period of time usually a year.
- ***The expenditure approach*** measures GDP as the total spending on final goods and services produced within a nation during a specific period of time usually a year. It is assumed that any good or service produced by an economy will also be purchased or used by someone. It is measured by adding the four major categories

of expenditures: consumption by domestic households, investment including fixed business, residential, and inventory investment, government purchases, and net exports (exports minus imports).

- ***The income approach*** measures GDP by summing up all incomes received in an economy during a specific period of time usually a year. These incomes include, among others, taxes paid to the government, corporate profits, and compensation of employees.

In theory, each of these approaches should lead to the same result, so if the output of the economy increases, incomes and expenditures should increase by the same amount. The problem here however, is that when using market prices to calculate GDP, inflation rates should be considered especially for those countries that have high and persistence inflation rates like the less developed countries.

SELF-ASSESSMENT EXERCISE

i. Illustrate the different methods of measuring economic growth.

3.5 The Components of Economic Growth

The sources of economic progress can be traced to a variety of factors, but, investments that improve the quality of existing physical and human resources, increase the quantity of these same productive resources, and raise the productivity of all or specific resources through invention, innovation, and technological progress have been the primary factors in stimulating economic growth in any society. We will briefly discuss these factors:

(i). Capital Accumulation

Capital accumulation is when some proportion of present income is saved and invested in order to add new resources, or upgrade the quality of existing resources. It involves a trade-off between present and future consumption that is, giving up a little now so as to have more in the future (Todaro & Smith, 2015). For instance, acquiring new factories, plants and equipment, machinery and materials can increase the capital stock of a nation and make it possible for output to be expanded. According to Metu et al. (2017) these

productive investments are supplemented by investments in socio-economic infrastructure such as energy, roads, portable water, communications, etc. For instance, a farmer who invest in a new tractor may increase the total output of the crops he can produce, but without adequate good road network to get this extra product to the markets, the investment may not add to food production.

Similarly, investment in human resources can improve its quality and thereby have the same or even a more powerful effect on production. Formal schooling, vocational and on-the-job training programs, and other types of informal education as well as direct investments in buildings, equipment, and materials may all be made more effective in augmenting human skills. All of these phenomena and many others are forms of investment that lead to capital accumulation.

(ii). Population and Labor Force Growth

Population growth, and the associated increase in the labor force, are considered positive factor in stimulating economic growth. A larger labor force means more productive workers, and a large overall population increases the potential size of domestic markets. However, it is questionable whether rapidly growing supplies of workers in developing countries with a surplus of labour exert a positive or a negative influence on economic progress. Obviously, it depends on the ability of the economic system to absorb and productively employ these added workers.

Given an initial understanding of these first two fundamental components of economic growth, the production possibility curve shows how a society can expand its potential total output with a given level of technology, physical and human resources.

Figure 1 shows two production possibility curves for two commodities *X* and *Y*. Initial possibilities for the production of *X* and *Y*are shown by the curve *PP*. Now suppose that without any change in technology, the quantity of physical and human resources were to double as a result of either investments that improved the quality of the existing resources or investment in new resources—land, capital, and, in the case of larger families, labor.

The figure shows that this doubling of total resources will cause the entire production possibility curve to shift uniformly outward from *PP* to *P′P′*. More of the commodities can now be produced.

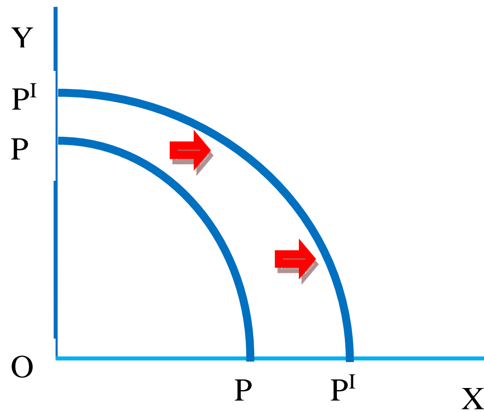

Figure 1: Production possibility curve for commodity X and Y

(iii) Technological Progress

Many economists consider technological progress as the most important source of economic growth. Technological progress is the increased application of new scientific knowledge in the form of inventions and innovations with regard to both physical and human capital.

There are three basic classifications of technological progress: Neutral, labour-saving, and capital-saving.

- **Neutral technological progress** occurs when higher output levels are achieved with the same quantity and combinations of factor inputs. In terms of production possibility analysis, a neutral technological change that, say, doubles total output is conceptually equivalent to a doubling of all productive inputs.

- **Labour-saving technological progress** is the achievement of higher output using an unchanged quantity of labor inputs as a result of some invention (e.g., the computer) or innovation (such as assembly-line production). Technological

progress since the late nineteenth century has consisted largely of rapid advances in labour-saving technologies for producing everything from beans to bicycles to bridges (Todaro & Smith, 2015).

- **Capital-saving technological progress** results from some invention or innovation that facilitates the achievement of higher output levels using the same quantity of inputs of capital. In the labor-abundant (capital-scarce) developing countries, however, capital-saving technological progress is what is needed most. Such progress results in more efficient (lower-cost) labor-intensive methods of production. For example, hand- or rotary-powered weeders and threshers, for small-scale agriculture. The indigenous development of low-cost, efficient, labor-intensive (capital-saving) techniques of production is one of the essentials of economic growth in developing countries.

Technological progress may also be labour- or capital-augmenting.

- **Labour-augmenting technological progress** occurs when the quality or skills of the labour force are upgraded, for instance, by the use of videotapes, televisions and other electronic communications media for classroom instruction.
- **Capital-augmenting technological progress** results in the more productive use of existing capital goods, for example, the substitution of steel for wooden plows in agricultural production.

SELF-ASSESSMENT EXERCISES

i. Identify the sources of economic growth in Nigeria.
ii. Discuss the difference between labour-saving technological progress and labour – augmenting technological progress.

4.0 CONCLUSION

The study of development economics is necessary because the principles are key to the design of successful economic development policy and programs. The field of economic development is versatile and has much to contribute regarding the problems of underdevelopment.

Economic growth as stated is the increase in the total amount of the goods and services (output) produced in an economy over time. Economic growth provides a necessary, although not sufficient condition for the development of an economy - without growth, there will be no development. Therefore, the study of economic growth is very necessary for understanding development issues in an economy. Economic growth is not just studied for the sake of output increase, but for a general progress in the economy.

5.0 SUMMARY

In this unit, we studied the nature of development economics and we also discussed the reasons why we need to study the course development economics. We also discussed economic growth, different ways of measuring economic development and the sources through which countries can accelerate economic growth.

6.0 TUTOR-MARKED ASSIGNMENTS

i. Aside getting a good grade, what do you hope to gain from the study of development economics?
ii. There are different methods of calculating economic growth rate in an economy. Identify and elaborate these different methods.
iii. What are the major sources of economic growth in Nigeria?
iv. Outline the three basic classifications of technological progress

7.0 REFERENCES/FURTHER READINGS

Haller, A. (2012). Concepts of economic growth and development: Challenges of crises and of knowledge. *Economy Trans-disciplinary Cognition, 15*(1), 66-7.

Jhingan, M. L. (2011). *The economics of development and planning, (40th ed.).* Delhi: Vrinda Publications (P) Ltd.

Kuznets, S. (1973). Modern economic growth: Findings and reflections. *The American Economic Review*, 63(3).

Mladen, M. I. (2015). Economic growth and development. *New technologies international, 3*(1), 55-62.

Metu, A. G. (2017).Economic growth and development. In U. R. Ezenekwe, K. O. Obi, M. C. Uzonwanne & C. U. Kalu (Eds). *Principles of economics II.* (164 - 178). Nigeria: Djompol Printers & Publishers.

Romer, P. (2007). From the Concise Encyclopedia of Economics. D. R. Henderson, (Ed.), *Liberty Fund*. *www.ecolib.org/library/Enc /Economic Growth.*

Todaro, M. P. & Smith, S. C. (2015). *Economic development*, *12th Edition*. Boston: United States of America. Pearson publishers

UNIT 2 CONCEPT AND MEASUREMENT OF ECONOMIC DEVELOPMENT

CONTENTS

1.0 Introduction
2.0 Objectives
3.0 Main Content
3.1 Meaning of Economic Development
3.1.1 The Orthodox or Traditional View
3.1.2 The New or Modern View
3.2 The Core Values of Economic Development
3.3 Measurement of Economic Development
3.4 Differences between Economic Growth and Development

4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References/Further Readings

1.0 INTRODUCTION

Economic growth as earlier discussed in the previous unit is increase in output (GDP), and is measured in monetary terms. To the neoclassical economists, economic growth is the same thing as development, but the development economists gave a different view about development. Economic development is the sustainable increase in the total outputs of goods and services produced in an economy accompanied by desirable institutional and social changes. This means that development cannot occur without economic growth. Hence, in this unit, we examine the concept of development, how to measure economic development as well as the differences between economic growth and development.

2.0 OBJECTIVES

At the end of this unit, it is expected that you should be able to:

- Discuss the meaning of economic development
- Enumerate the core values of economic development
- Explain how economic development is measured
- Differentiate between economic growth and development.

3.0 MAIN CONTENT

3.1 The Meaning of Economic Development.

The term *development* means different things to different people. The failure to agree on what constitutes development and how it could be effected has its roots on what the concept is. The meaning of development in this context, requires some in-depth study and research so that countries at the different levels of development can truly understand what it means. Hence, the meaning of development will be discussed under two approaches - the orthodox or traditional view of development and the alternative or new view of development.

3.1.1 Traditional or Orthodox view of Development

The period between 1950 and 1970s was dominated by the traditional or orthodox view of development. To the traditional view, economic development was based on an increase in output, measured by the **gross domestic product (GDP)**. Development was meant to achieve sustained growth rates of **income per capita** to enable a nation to expand its output at a rate faster than the growth rate of its population. The rates of growth of real per capita **gross national income (GNI)** (monetary growth of GNI per capita minus the rate of inflation) were then used to measure the overall economic well-being of a population (Todaro & Smith, 2015). This means that economic development depends on how much of real goods and services is available to the average citizen for the purpose of investment and consumption. To the orthodox economists, the problems of poverty, unemployment, and income distribution were of secondary importance. Development policies were formulated with the belief that per capita GNI growth would either trickle down to the masses in the form of jobs and other economic opportunities or create the necessary conditions for the wider distribution of the economic and social benefits of growth. Within the orthodox view, the Western nations were the defining platform for development. This means that development is a situation where developing countries would replicate the Western development experience.

The conceptual framework of the orthodox economic view provides a useful analytical tool for understanding the concept and consequence of development, but did not shed light on the socio-economic progression of development (Onwuka, 2013 as cited in Metu et al., 2017). This means that the framework is inadequate in explaining the vital issues related to development problems. It was based on this shortcoming that development economists came up with what is regarded as the alternative view of development.

3.1.2 The New Paradigm View of Economic Development

The new paradigm view of economic development was formulated due to experience of the first decades of post– Second World War and postcolonial development in the 1950s, 1960s, and early 1970s. During those periods, many developing nations reached their economic growth targets while the standard of living of majority of the masses remained unchanged. This showed that something was wrong with the narrow definition of development as rendered within the orthodox paradigm. For instance, a number of developing countries experienced relatively high rates of growth during the 1960s and 1970s with little or no improvement or even any actual decline in employment, equality, and the real incomes of the bottom 40% of their populations (Onwuka, 2011).

In the 1980s and 1990s the situation worsened as GNI growth rates in many developing countries declined, which lead governments to borrow and were forced to cut back on their already limited social and economic programs. Economic development came to be redefined, in the 1970s, in terms of the reduction or elimination of poverty, inequality, and unemployment within the context of a growing economy. According to Todaro and Smith (2015: 18) Dudley Seers posed the question and ased: "What has been happening to poverty? What has been happening to unemployment? What has been happening to inequality? If all three of these have declined from high levels, then beyond doubt this has been a period of development for the country concerned. If one or two of these central problems have been growing worse, especially if all three have, it would be strange to call the result development even if per capita income doubled"

Economic development is not about index numbers of national income neither is it about savings and investment ratios, it involves identifying the basic needs of human beings so as to raise their standard of living. Hence, Jhingan (2007) defined development as economic growth plus change. This means that development leads to qualitative changes in the entire social system so as to improve the lives of the people. Development is a multidimensional process involving the improvement of economic growth and major changes in social structures, popular attitudes, and national institutions, the reduction of inequality as well as the eradication of poverty (Todaro & Smith, 2015). Development represents the whole scope of change in an entire social system, where individuals and social groups, moves away from a condition of life widely perceived as unsatisfactory towards a situation or condition of life regarded as materially and spiritually better.

SELF-ASSESSMENT EXERCISE

i. Explain the orthodox view of economic development.
ii. How did the new paradigm view economic development?

3.2 The Core Values of Economic Development

Economic development is conceptualized as the sustained elevation of an entire society and social system toward a more humane life. The issue of what constitutes the good life is a question that must constantly be reevaluated. Todaro and Smith (2015) identified three basic components or core values for understanding the inner meaning of development. These core values namely life sustenance, self-esteem and freedom from servitude are well explained thus:

- **Life Sustenance** is the improvement in socioeconomic environment so that individuals will meet up with basic needs of life like food, shelter, clothing, education, health and protection. One of the basic functions of the government is to provide the means of overcoming misery and helplessness to as many in the society as possible. Economic development is a necessary condition for the improvement in the quality of life of the citizens, which cannot be achieved without a sustained economic progress.

- **Self-esteem** is the sense of self-worth as well as self-respect where one cannot be used as tool by others to satisfy personal end. Societies and individuals seek some self-esteem in form of self-respect, identity, honour and dignity. Though the nature of this self-respect differs according to culture even though most societies suffer serious cultural confusion due to modernization and globalization. Development should be a goal of any society because it is an indispensable way of gaining self-esteem.
- **Freedom from servitude** is the ability of societies and individuals to make choices and be free from dissatisfying material conditions of life. Freedom as used in the development context is the total emancipation from oppressive institutions, misery and dogmatic beliefs. Freedom involves a wide range of choices for the people as well the reduction of external constraints in the pursuit of development. There is need for freedom to have more goods and services, freedom of expression, political freedom, including personal security, the rule of law and equality of opportunity.

Development problem is a human problem on how to ensure a progressively rising standard of living. Recently, the concept of economic development does not only involve reduction in poverty, unemployment and inequality but has been widened to include improvement in quality of life with cleaner environment, good health and nutrition, better education and equality of opportunities (Metu et al., 2017).

SELF-ASSESSMENT EXERCISE

i. List and explain the core values of economic development?

3.2 The Measurement of Economic Development

Growth in national income or per capita income which is an indicator of economic growth does not represent an adequate measure of welfare and economic development. Scholars are interested in the measurement of economic development particularly for comparing development among countries. The criteria by which development is to be

judged are qualitative criteria. Criteria such as the standard of living, the educational level and extent of participation in the development process cannot be directly measured rather they can be measured using measurable quantitative indicators (Ahuja, 2016). The United Nations in 1990 came up with the traditional Human development index (HDI). But, in November 2010, the traditional HDI was replaced with a New Human Development Index (NHDI). The NHDI, ranks countries on a scale of 0-1 (lowest to highest human development) based on three goals of development: *A long and healthy life (*measured by life expectancy at birth); *knowledge* (measured by combining average schooling attained by adults and expected years of schooling for school-age children); and a *decent standard of living* (measured by real per capita gross domestic product adjusted for the differing purchasing power parity of each country's currency).

The United Nations uses the HDI to rank economies into four groups: (i) low human development (0.0 - 0.535), (ii) medium human development (0.536 - 0.711), (iii) high human development (0.712 - 0.799), and (iv) very high human development (0.80 - 1.0). The calculation of the NHDI is illustrated using a hypothetical data for Nigeria

3.2.1 Calculating the Human Development Index

Calculating the HDI requires calculating the indices for each of the dimensions: Life Expectancy Index, Education Index and Gross National Income adjusted for Purchasing Power Parity Index and defining relevant minimum and maximum values (or lower and upper goalposts) for each indicator as show in Table 1

Table 1: Goalposts for Calculating the HDI

Indicator	**Maximum Value**	**Minimum Value**
Life Expectancy at Birth (yrs)	83.57	20
Mean Years of Schooling	13.3	0
Expected Years of Schooling	18	0
GNI per capita (PPP US$)	$87,478	$100

Source: Todaro and Smith, (2015)

Performance in each dimension is expressed as a value between 0 and 1 by using this formula:

$$\text{Dimension index} = \frac{\textit{Actual Value - Minimum Value}}{\textit{Maximum Value - Minimum Value}}$$

This means that the component indexes of the NHDI are computed by taking the difference between the country's actual achievement and the minimum goalpost value, and then dividing the result by the difference between the overall maximum goalpost and minimum goalpost values.

The *HDI* is then calculated with the geometric mean thus:

$$\text{New Human Development Index} = \sqrt[3]{H * E * I}$$

Where, *H* stands for the health index, *E* stands for the education index, and *I* stands for the income index.

Let us take an example:

Given the hypothetical data below, calculate the HDI for Nigeria for the year 2013.

What income group does Nigeria belong to?

Indicator	Value
Life expectancy at birth (years)	64.6
Mean years of schooling	7.0
Expected years of schooling	11.4
GNI per capita (PPP $)	1,684

Solution:

The health dimension which is measured by life expectancy at birth index, takes a minimum value of 20 years and a maximum value of 83.57 years. Using our Nigerian hypothetical data:

$$\text{Life expectancy index} = \frac{64.4-20}{83.6-20} = 0.701$$

The education component of the HDI is calculated with a combination of the average years of schooling for adults aged 25 and older and expected years of schooling for a school-age child now entering school. These indicators are normalized using a minimum

value of 0, and maximum value of mean years of schooling is 13.3 years. For our example, calculating the sub index, using our hypothetical data, 7yrs is the average years of schooling among adults,

The mean years of schooling $= \frac{7.0-0}{13.3-0} = 0.527$

The maximum value for expected years of schooling is given as 18 years. Now if our estimated value for expected years of schooling is 11.4 years, then the sub index is,

Expected years of schooling $= \frac{11.4-0}{18.0-0} = 0.634$

Therefore, the education index will be the geometric mean of the two sub-indexes.

Education index $= \frac{\sqrt{0.527*0.634-0}}{0.971-0} = 0.596$

The standard of living (income) component is calculated using purchasing power-adjusted per-capita gross national income (GNI). Therefore,

Income index $= \frac{\ln(1,684)-\ln(100)}{\ln(87,478)-\ln(100)} = 0.417$

Then in calculating the overall index, a geometric mean of the three indices is used as shown below:

Therefore, the HDI $= \sqrt[3]{0.701 * 0.598 * 0.417} = 0.596$

Since the HDI falls within0.536 - 0.711, we can say that Nigeria belongs to medium human development category.

SELF-ASSESSMENT EXERCISE

i. Why is gross domestic product not a good measure of economic development?
ii. If a country's life expectancy at birth is 78years, mean-years of schooling is 8years, expected-years of schooling is 12years and the GNI per capita (PPP US$) is $8,840. Calculate the HDI for the country.
iii. The country identified in Question (ii) comes under what category of human development?

3.3 The Differences between Economic Growth and Development

Some of the major difference between economic growth and economic development are:

(i). Economic growth may be defined as a sustained increase in aggregate output or supply of goods and services while economic development is defined as economic growth accompanied by desirable social changes in a way that there is progress in all human endeavours (Metu et al., 2017).

(ii). Economic growth and economic development have different indicators for their measurement. Economic Growth can be measured through an increase in the GDP and per capita income. However, economic development can be measured through improvement in the life expectancy rate, infant mortality rate, literacy rate, and poverty rates.

(iii). Economic growth does not consider the unrecorded income from economic activities in the informal sector in most cases. Whereas, economic development takes into consideration economic and non-economic activities.

(iv). Economic growth does not capture the depletion of natural resources through pollution, congestion and diseases. But, economic development is concerned with sustainability that is, meeting the needs of the present generation without compromising the needs of future generation. Sustainability is necessary because governments are under pressure due to the environmental issues caused by Global warming and man's activities.

(v). Economic growth is a subset of economic development, this means that economic growth is very necessary for achieving economic development in an economy(vi). The process of economic growth is automatic and happens within a short period of time. Economic development is a continuous process, the outcome is as a result of planned and result-oriented activities after achieving growth.

SELF-ASSESSMENT EXERCISE

i. Outline the differences between economic growth and economic development.

4.0 CONCLUSION

Economic development is economic growth accompanied by desirable social changes. Economic growth is necessary for development but does not guarantee it. That is, without economic growth, development cannot occur because rising incomes are needed for improved welfare as well as in developing social services in an economy. Economic growth and development should not be used interchangeably because economic growth is measured using GDP while economic development is measured using a composite of three indicators namely standard of living, knowledge and health.

5.0 SUMMARY

This unit discussed extensively the concept of economic development in the context of orthodox and new views of development. We also discussed how economic development is measured using the New Human Development Index and concluded by differentiating economic growth from economic development.

6.0 TUTOR-MARKED ASSIGNMENTS

i. Explain what you understand by economic development.
ii. Use a hypothetical data and compare the HDI of Ghana and the USA.
iii. Identify reasons why economic growth may happen without development in an economy.
iv. Should economic growth be used interchangeably with economic development? Justify your answer.

7.0 REFERENCES/FURTHER READINGS

Ahuja, H. L. (2016). *Development economics*. New Delhi: S. D. Chand.

Hicks, N. & Streeten, P. (1979). Indicators of development: The search for a basic need yardstick. *World Development,* 7(6), 568-580. www.DOI:10.1016/0305750X(79)90093-7

Jhingan, M. L. (2007). *The economics of development and planning, (39th ed.).* Delhi: Vrinda Publications (P) Ltd.

Metu, A. G. (2017).Economic growth and development. In U. R. Ezenekwe, K. O. Obi, M. C. Uzonwanne & C. U. Kalu (Eds). *Principles of economics II.* (164 - 178). Nigeria: Djompol Printers & Publishers.

Mladen, M. I. (2015). Economic growth and development. *New technologies International, 3*(1), 55-62.

Onwuka, C. E. (2011). *Economic development monograph series 3*.Ekpoma: Pon Publishers

Todaro, M. P. & Smith, S. C. (2015). *Economic development*. *12th Edition*. USA: Pearson Publishers.

UNDP, (2017). The real wealth of nations: Pathways to human development. *Human Development Report 2017.*

UNIT 3 DEVELOPMENT AND UNDERDEVELOPMENT

CONTENTS

1.0 Introduction
2.0 Objectives
3.0 Main Content
    3.1 Meaning of Underdevelopment
    3.2 Common Characteristics of Developing Countries
    3.3 Major Obstacles to Economic Development
    3.4 Major Determinants of Economic Development
4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References/Further Readings

1.0 INTRODUCTION

All economies of the world are not equally developed. Some are more developed than others. Hence, the economies of the world are being classified as either developed or underdeveloped. In this unit, we discuss the meaning and characteristics of underdevelopment in order to enable us understand the basis for the classification of economies. There are many obstacles that inhibit underdeveloped economies from achieving development, but in this unit, we look at some of the major obstacles. You are expected to consult the references at the end of this unit to guide you in identifying other obstacles that are not added in this unit.

2.0 OBJECTIVES

At the end of this unit, it is expected that you should be able to:

- Discuss the meaning of underdevelopment
- Explain the common characteristics of underdevelopment
- Identify the major obstacles to economic development
- Enumerate the determinants of economic development

3.0 MAIN CONTENT

The HDI is used to determine if a country is developed or underdeveloped. Developed countries (economies) are highly industrialized countries while developing countries are not. The developing countries are also referred to as less developed countries (LDCs) with certain characteristics that are common to them and qualifies them as such. They are usually nations with low Human Development Index (HDI) relative to thedeveloped countries. In this unit we will discuss the meaning and characteristics of underdevelopment in order to know whether a country is developed. We will also discuss the major obstacles faced by developing countries in their quest for development.

3.1 Meaning of the Term Underdevelopment

Countries of the world are not equally developed, hence, the classification into developed and underdeveloped economies. In past years, the underdeveloped economies were called backward or third world countries, while the developed economies were referred to as advanced economies. But, recently, the terms backward, third world and advanced are considered unsatisfactory and misleading, hence, they are replaced with the terms underdeveloped and developed economies. According to Todaro and Smith (2015) underdeveloped economy is that economy with low levels of living, absolute poverty, high birth and death rates, and over dependence on foreign countries. Similarly, the United Nations describe an underdeveloped country as one with low per capita income in comparison to per capita real income of some advanced countries such as USA, Canada, and Western Europe. By implication, this means that underdeveloped countries are poor with unutilized natural resources.

By the United Nations classification, underdeveloped countries are classified as developing economies, which implies that the process of development have been initiated in these economies (Ahuja, 1980). The World Bank divides the developing countries into low income and middle income countries. A developing economy (less developed economy) is an economy with an underdeveloped industrial base and a low human development index relative to other developed countries. In most developing economies,

rapid population growth is always a threat to economic development. Some developing countries exhibit strong economic growth and dynamics, while other countries stagnate. Underdevelopment can be defined by incidence of poverty, misdistribution of national income, by social disorganization and administrative incompetence (Jhingan, 2011).

SELF-ASSESSMENT EXERCISE

i. What do you understand by underdevelopment?

3.2 Common Characteristics of Underdevelopment

Developing countries differ from each other, but there are common features present in all the developing countries and they are:

(i). General Poverty- Developing countries are caught in what Nobel laureate Gunnar Myrdal called circular and cumulative causation or poverty trap where, a vicious circle may set in. At very low income levels there will be low investment in education and health as well as plant and equipment and infrastructure, which in turn leads to low productivity and economic stagnation. Further, the low-income countries are themselves a very diverse group with greatly differing development challenges.

(ii). Peasant Agriculture System – Most low-income countries are predominantly peasant agricultural societies whose main concern is for survival. The agricultural activities in underdeveloped countries are usually subsistence farming with low output. There is also heavy concentration of people in the agriculture sector which is a symptom of poverty (Jhingan, 2011). Such countries also specialise in the production of primary products such as raw materials and foodstuffs. For instance, Nigeria produces crude oil and sell to developed countries. Those who produce foodstuffs have poor storage system resulting to a lot of wastages. The agricultural tools are more of local tools leading to low productivity when compared to the developed countries such as USA.

(iii). Inadequate Capital – In underdeveloped countries, there is insufficiency of capital equipment. The high rate of poverty makes it difficult to save. When savings is low, there will be low investment and poor capital stock. The low rate of growth of capital stock can

hardly provide for the rapidly growing population let alone for investments in capital projects. For instance, gross investment in underdeveloped countries is below 6% while in developed countries it is above 20% (Jhingan, 2011). The rate of capital deficiency in developing countries can be attributed to low per capita income, people on subsistence level finds it difficult to save thereby leaving very little for investment. Another reason is because of what is called the 'demonstration effect' where people increase their consumption pattern trying to emulate the life style or standard of living in advanced countries. As a result, income is spent on increase consumption, thus savings become static or negligible.

(iv). Underdeveloped Natural Resources – Most underdeveloped economies have natural resources such as land, water, forest, iron, petroleum, tin, etc.; that are either unutilized or underutilized. This could be as a result of various inhibitors such as low demand due to small extent of the market, inaccessibility, non-availability of capital formation and lack of technical know-how.

(v). High Level of Unemployment and Underemployment – Unemployment is a situation where people who are willing to work do not find work. Underemployment is where an individual is working but below his/her capacity/qualification. In underdeveloped economy, unemployment and underemployment is involuntary because employment opportunities are limited in respect to the number of people willing to work. There are also those who work full time in terms of hours per day but earn very little to rise above the poverty level. They are hawkers, petty traders, hotel workers, etc.

(vi). Overdependence on International Trade - A number of developing countries are highly dependent on international trade and subject to volatile export earnings. Several low-income countries and oil exporting countries depend a great deal on a few commodities or countries for export sales. Foreign trade orientation manifest through the flow of foreign capital to underdeveloped countries. It plays significant role in developing and expanding the export sector; and such a widespread hold of foreign capital drains the resources of underdeveloped countries.

(vii). A Dual Economy– Most underdeveloped economies have this dualistic structure. One is the market economy and the other is subsistence economy whereby the modern system of activity conflicts with the traditional system and the ability to manage them pose a very big problem. This structure also leads to a situation whereby one aspect is superior to the other. The market economy is highly industrialized and centered in the towns with modern amenities such as buildings, banks, government offices, etc. The subsistence economy is backward and is mainly agriculture oriented. The dualistic nature of the economy is not conducive to healthy economic progress because the primary sectors limits the development and expansion of both the primary and secondary sectors.

(viii). Rapid Population Growth - Whereas the population growth rate in industrialized countries has continued to decline, Developing countries birth rates remained at high levels, resulting in an annual growth of 1.6% (Nafziger, 2006). High fertility means that a high percentage of the population are in dependent ages, 0–14, leading to the diversion of resources to food, shelter, and education for a large nonworking population. The under-5 mortality is much higher in low income countries than in high income countries, although great progress has been made since 1990. The problem in LDCs is not rapid population but low productivity (low levels of technology and capital per worker) combined with rapid population growth.

(ix). Poorly Developed Economic and Political Institutions–According to IMF (2003) institutional development measures the quality of governance, public sector efficiency, the level of corruption, political rights, and regulatory burdens. The institutions consist of the formal rules (constitutions, common law and regulations), the informal constraints (norms, conventions, and codes of conduct), as well as the enforcement units. Many developing countries lack the economic institutions and governance structures needed to attract both domestic and foreign private investment.

SELF-ASSESSMENT EXERCISE

ii. Describe the term underdevelopment
iii. Outline the characteristics of an underdeveloped economy.

3.3 Differences between a Developed and an Underdeveloped Country

Figure 2a: Underdevelopment

Source: Business Day Newspaper (July 16 2019); The Guardian Newspaper (June, 2018)

Figure 3b: Development

Source: Quora.com

Table 2: Developed and Developing Countries Compared

Basis of Difference	Developed Country	Developing Country
Definition	Developed countries are countries that are more industrialized with highly advanced technological infrastructures. Some developed nations include the United States, Canada, Japan, Republic of Korea, Australia, New Zealand and countries of Western Europe	Developing countries are poor agricultural country that seeking to become more advanced economically and socially. Less developed countries are found in Africa, India, and other countries in southern Asia.
National wealth and Standard of living	More average income, higher per capita income and better standard of living	Low average income, less per capita income and low standard of living
Character of the economy	Literacy rate is quite high due to better education system. Life expectancy rate is more due to better standard of living	Literacy rate is quite low as people are deprived of education facilities. Life expectancy rate is low due to poor health facilities.
Factors of production	Well developed and effectively used leading to high labour productivity	Low or Moderate and ineffectively utilized, hence, low productivity
Growth rate of Population	Low rate of population growth rate and low dependency burden	High rate of population growth with high dependency burden
Nature of production	Diversified economy with emphasis on manufacturing sector and importation of primary products from developing countries	Dependent on primary export sector with foreign exchange earning being spent on importation of finished or semi-finished goods
Cultural environment	Materialistic cultural environment with high dignity of labour.	Cultural environment is more of spiritualism and there is low dignity of labour.
Perspective of growth	Very high due to capital accumulation and technological progress. Outlook is progressive.	Low due to absence of proper institutional and structural arrangements.

		Outlook is backward.

Source: www.researchgate.net

3.4 Obstacles to Economic Development

The basic characteristics of underdeveloped countries earlier discussed might as well be regarded as the obstacles to their economic development. They help to answer the broad question of why a poor country is poor. The factors that inhibit economic development are:

(i). The Vicious Cycle of Poverty – One of the widely propagated reasons for underdevelopment is the trap in the vicious cycle of poverty. A vicious cycle is where one problem begets another problem and causes the first problem again and the process is repeated over and over again. Economists use the vicious cycle of poverty to simply explain the reason for underdevelopment, that is poverty begets poverty and binds populations in poverty unless there is an external intervention to break the cycle. The situation in underdeveloped countries is such that the per capita income of populations is low and leads to low savings. Low savings will lead to low investment and low productivity. Low production leads to low income and hence the cycle repeats itself. Hence underdeveloped countries are poor because they lack enough capital for investment. Capital is a key recipe for economic development and a country that is starved of it is trapped in its own poverty hence the saying a country is poor because it is poor. An economy can come out of poverty if capital formation rate increases more than the population growth. Therefore, capital formation spurs economic development by demand and supply of capital (Pragyandeepa, 2015). The vicious cycle can be explained from the demand side and supply side as is explained in Figure 3.

Supply side of the vicious circle of poverty shows that productivity is low due to low capital formation and low real income. This means that the capacity to save is low leading to low level of national income. The low real income is a reflection of low productivity which is mainly caused by insufficient capital. Low income results from low saving capacity and hence the circle completes. In other words, the underdeveloped

countries cannot develop because their rate of production is low hence they have nothing to spare for capital formation which is necessary in raising their living standards. In the economy, investment is not only determined by saving but also on the ability and willingness to invest. The attitude of the rich class in underdeveloped economies is not to dare take risks. The medium income group prefer to work in trades, services etc. instead of capital creation. This is due to lack of investment capital, limited industrial finance, insufficient skilled labour, social overhead, etc.

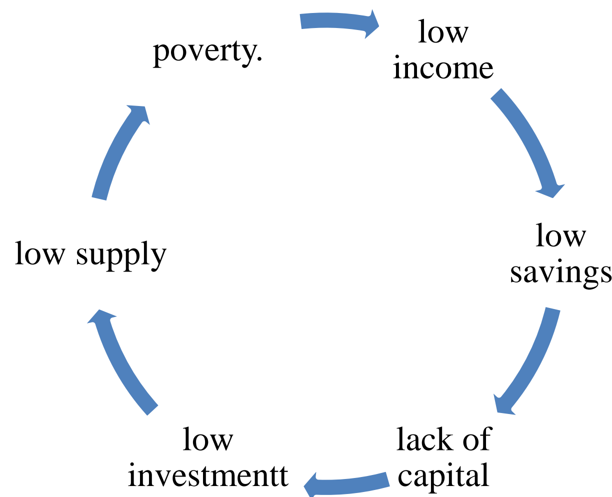

Figure 3a: The supply side of the vicious cycle of poverty

Source: VioMLetty, (2016)

Demand side of the vicious cycle of poverty shows that the inducement to invest in an economy may be low because of low purchasing power of the people. In underdeveloped countries production is normally low. This leads to low per capita income and low purchasing power. The low purchasing power limits the demand for goods and services. Low demand limits the market. The limited market leads to low inducement to invest which leads to low production. The low production results to low production per capita. This in turn leads to low per capita income. Therefore, the vicious circle of poverty closes on the demand side.

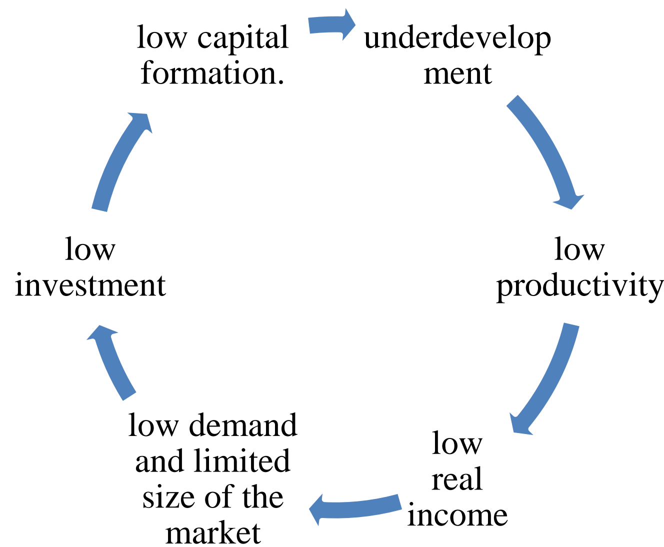

Figure 3b: The demand side of the vicious cycle of poverty

Source: VioMLetty, (2016)

The vicious cycle can be broken in underdeveloped economies by making large investment in a different import-substituting industries and by producing for export. In this way, growth can be accelerated to raise the standard of living of the people. For instance, East Asian countries used this route to accelerate their economic growth.

(ii). Imbalance between Capital and Population – One of the most serious problems affecting underdeveloped economies is the imbalance between resources and population. The current stock of capital is not sufficient enough to employ all at the level of real per capita income. Population growth is not really a problem to economic development but a means to achieving development if well managed. Where population becomes a problem is when the capital stock is not adequately balanced with the population. If the population grows faster than the stock of capital of a country, the additional labour force will not be duly employed due to low instruments for production. Tackling the problem of imbalance between capital and population should be a long term projection. A nations stock of capital can be increased through investment and capital formation. The rate of capital formation needs to be kept so that employment opportunities are successively enlarged to

absorb the increased labour force. Also, when investment increases it leads to specialization and employment for the growing population.

(iii). Deficiency of Dynamic Entrepreneurship – Innovative entrepreneurship leads to development. Underdeveloped economies practice imitative entrepreneurship that is, imitating the developed economies instead of developing new ideas for themselves. What underdeveloped economies need is innovative entrepreneurs to bring out new ideas and move their nation towards the Fourth Industrial revolution where specialization is the order of the day.

(iv). Demonstration Effect–Demonstration effect is when your actions depend on the actions of others. Demonstration leads to imitation and imitation of superior consumption standard stimulates consumption among the poor which increase their propensity to consume and consequently reduce their capacity to save. Demonstration can be seen when developed countries pass to the underdeveloped countries their consumption pattern. This aggravates propensity to consume and reduces capacity to save which is an impediment to economic development. Demonstration effect can also be felt when the actions of underdeveloped countries depend on the actions undertaken by the developed countries. The underdeveloped countries copy the policies, life style and way of life of the developed countries thereby making them over dependent on the developed world. It may also be due to the allurement of superior levels of living. This throws new light on international economic relations (Ahuja 1980). Relationships with other countries may bring prosperity or create difficulties, for instance consumption in developed countries may increase consumption and hinder capital formation in underdeveloped countries.

Underdeveloped countries can overcome demonstration effect by curtailing the consumption of luxury goods so as to divert resources towards productive activities.

(v). Inadequate Infrastructure – Economic growth and development in developing countries have been impeded by inadequate infrastructure such as health and education facilities, transportation, power, communication as well as credit facilities to business enterprises. Electricity is used for all productive activities and lowers industrial and

agricultural development when in short supply. Also, good transportation system is needed to transport raw materials and finished products, thereby widening the market for goods and services. Similarly, entrepreneurs and even farmers needs credit facilities to start or expand their productive activities. The availability of these infrastructural facilities encourages and facilitates production in industry, agriculture and other productive sectors. Therefore, the government should give priority to providing and expanding the infrastructural facilities in developing countries.

(vi). Socio-Cultural Constraints– Economic development has to do with human endowments, political conditions, social attitudes and institutions. There are also elements of social resistance to economic change which is not conducive for economic development UNDP, 2017). The social resistance includes institutional factors characterized by rigid stratification of occupations reinforced by traditional beliefs and values, differences in cultural tradition and social pattern, regional identifications, etc. All these factors inhibit social and geographical mobility and constitute a hindrance to progress. Family attitudes and attachment also put pressures on people and limit the range of individual freedom in making decisions regarding savings and investment. The people from such countries are opposed to accepting new values and innovations necessary for economic development.

(vii). Human Resource Constraint– One of the important obstacles to economic development in LDCs is undeveloped human resources. Developing countries possess large population with surplus labour but with limited critical skills and knowledge. The limited skills make it difficult for physical capital to be productively utilized and to wear out and breakdown easily; leading to fall in production quality as well as rise in costs. The undeveloped human resources manifest in or translate to low labour productivity, limited specialization, factor immobility and social institutions that minimise the incentives for economic development.

4.0 CONCLUSION

An underdeveloped economy is an economy with weak economic and development base. Although LDCs are diverse, they have some common characteristics that especially apply to low-income countries. Low-income economies tend to have a high percentage of production and labour force in agriculture, low savings rates and technology, relatively rapid population growth, relatively low literacy and skills, and poorly developed institutions. These characteristics can be regarded as the obstacles to their achieving development. A number of these characteristics are both cause and consequences of poverty.

5.0 SUMMARY

In this unit, we discussed the meaning of underdevelopment and the characteristics of underdevelopment. Factors such as demonstration effect, inadequate infrastructure, vicious cycle of poverty and low capital formation are some of the obstacles hindering the development of underdeveloped economies.

6.0 TUTOR-MARKED ASSIGNMENTS

i. Differentiate between development and underdevelopment.

ii. Explain the vicious cycle of poverty.

iii. Identify the obstacles to hindering Nigeria from achieving economic development.

iv. How can the Nigerian government overcome the obstacles identified in Question

7.0 REFERENCES/FURTHER READINGS

Ahuja, H. L. (21980). *Modern economics*. New Delhi: S. D. Chand

Ahuja, H. L. (2016). *Development economics*. New Delhi: S. D. Chand

Business Day Newspaper (July, 2019). Retrieved from https://businessday.ng/columnist/article/culture-a-necessity-to-overcome-underdevelopment-2/

Olajide, O. T. (2004). *Theories of economic development and planning*. Lagos: Pumark Nigeria Ltd.

Metu, A. G. (2017).Economic growth and development**.** In U. R. Ezenekwe, K. O. Obi, M. C. Uzonwanne & C. U. Kalu (Eds). *Principles of economics II.* (164 - 178). Nigeria: Djompol Printers & Publishers.

Nafziger, E. W. (2006). *Economic development*. New York: Cambridge University Press

Romer, P. (2007). From the Concise Encyclopedia of Economics. D. R. Henderson, (Ed.), *Liberty Fund*. *www.ecolib.org/library/Enc /Economic Growth.* Accessed on 9/9/2013.

The Guardian Newspaper (June, 2018). Retrieved from https://guardian.ng/opinion/the-pains-of-underdevelopment/ June 11th

Todaro, M. P. & Smith, S. C. (2015). *Economic development*. 12thEdition. USA: Pearson Publishers.

UNDP, (2017). The real wealth of nations: Pathways to human development. *Human Development Report 2017.*

UNIT 4 ISSUES ON SUSTAINABLE DEVELOPMENT

CONTENTS

1.0 Introduction
2.0 Objectives
3.0 Main Content
- 3.1 Meaning of Sustainable Development
- 3.2 The Pillars of Sustainable Development
- 3.3 The Sustainable Development Goals
- 3.4 Policies on Sustainable Development

4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References/Further Readings

1.0 INTRODUCTION

Long before the late 20th century, scholars argued that there need not be a trade-off between environmental sustainability and economic development**.** Thenin 1987, the Bruntland Commission published its report, *Our Common Future*, in an effort to link the issues of economic development and environmental stability. In this unit, we adopt the United Nations (1992) definition of sustainable development to understand the meaning. We will also study the 17 goals and policies aimed at achieving the 2030 sustainable development.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- Discuss the meaning of sustainable development
- Outline the pillars of sustainable development
- Highlight the goals of sustainable development
- Explain policies on sustainable development.

3.0 MAIN CONTENT

3.1 Definition of Sustainable Development

Many definitions of sustainable development abound, but, the most often used definition is that proposed by the Brundtland Commission. It defined sustainable development as meeting the needs of the present generation without compromising the needs of the future generation. (Mensah, 2019). This concept of conserving resources for future generations is one of the major features that distinguish sustainable development policy from traditional environmental policy, which also seeks to internalize the externalities of environmental degradation.

According to Jhingan (2011) sustainable development means that development should keep going. This means that economic development does not decline over time but continues to contribute to the quality of life through improvement of the natural environment. The overall goal of sustainable development (SD) is the long-term stability of the economy and environment; this is only achievable through the integration and acknowledgement of economic, environmental, and social concerns throughout the decision making process.

Many of the challenges facing humankind such as climate change, inequality and hunger and water scarcity can be resolved at a global level by promoting sustainable development and guaranteeing the balance between caring for the environment, economic growth and social well-being. Sustainable development is a commitment to social progress, economic growth and environmental balance which are often referred to as the 3 pillars of stainable development.

SELF-ASSESSMENT EXERCISE

i. Discuss the meaning of sustainable development.

3.2 The Pillars of Sustainable Development

Sustainable development implies that the best choices are likely to remain those that meet the needs of society and are environmentally and economically viable, economically and socially equitable as well as socially and environmentally bearable. The three-

dimensional distinct but interconnected pillars – environmental stewardship, economic growth and social inclusion in Figure 4 recognizes that growth must be both inclusive and environmentally sound to reduce poverty and build shared prosperity for today's population and to meet the needs of future generation.

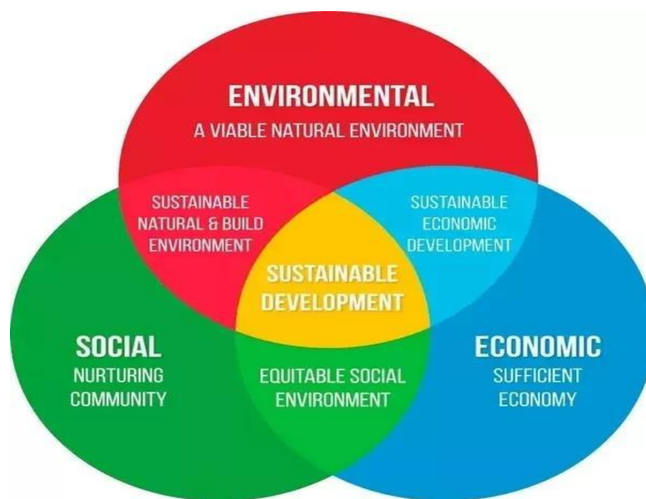

Figure 4: Economic, social and environmental sustainability.

Source:* *www.researchgate.net

(i). Economic Sustainability - Economic sustainability implies a system of production that satisfies present consumption levels without compromising future needs. Economists initially assumed that the supply of natural resources was unlimited and they placed undue emphasis on the capacity of the market to allocate resources efficiently (Du & Kang, 2016). They also believed that economic growth would be accompanied by the technological advancement to replenish natural resources destroyed in the production process. Recently, it has been realized that natural resources are not infinite; not all of them are renewable nor can be replenished. This has prompted many academicians to question the possibility of an uncontrolled consumption and growth process.

An economy consists of markets with different transactions. The three main activities being carried out in an economy are production, distribution and consumption, but the accounting structure being used to evaluate economic activities misrepresents values and

this does not augur well for society and the environment (Cao, 2017). Human life is maintained and supported by utilising the limited natural resources within the earth, but due to population growth, basic needs such as clothing, food and housing needed to maintain human life increases, without the available resources to meet the requirements forever. As the main concern of economies seems to be on economic growth, they ignore some cost components such as the impact of depletion and pollution, while increasing demand for goods and services continues to drive markets and infringe destructive effects of the environment. Economic sustainability, therefore, requires that decisions are made in the most equitable and fiscally sound way possible, while considering the other aspects of sustainability (Zhai & Chang, 2019).

(ii). Social Sustainability - Social sustainability includes empowerment, equity, accessibility, stability, participation and cultural identity (Daly, 1992). Social sustainability also includes human rights, gender equity, public participation and rule of law. Since development is about the people, it implies that people matter a lot. Basically, social sustainability indicates a system of social organization needed to ease poverty. Social sustainability relates to the relationship between social conditions such as poverty and environmental destruction. This means that the theory of social sustainability involves poverty alleviation without unnecessary destruction of the environmental nor economic instability. It is expected that poverty alleviation should be within the existing environmental and economic resource base of the society. Social sustainability is aimedat providing enabling environment for people to have the capacity to realize their needs, if they so desire. Hence, any obstacles toward achieving this capacity is considered a barrier that needs to be addressed so that social sustainability can be achieved by individuals, organizations or communities.

(iii). Environmental Sustainability - Environmental sustainability is concerned about the natural environment and how it remains productive and resilient to support human life. Environmental sustainability relates to ecosystem integrity and carrying capacity of natural environment (Brodhag & Taliere, 2006). It requires that natural capital be

sustainably used as a source of economic inputs. This means that natural resources must be harvested no faster than they can be renewed while waste must be emitted no faster than they can be adapted by the environment (Mensah, 2019). This is because the earth systems have limits or boundaries within which equilibrium is maintained.

Similarly, the quest for economic growth is imposing greater demands on the earth system and placing even greater strain on these limits because technological advancement may fail to support exponential growth (Mensah, 20119). The effects of climate change, is a good example why there is need for environmental sustainability. Climate change is the long-lasting changes in the climate system which is caused by human activities or by natural climate variability (Ahuja, 2016). The changes include global warming, rising sea level, increasing acidification of the oceans and increasing concentrations of greenhouse gases. Climate change has already shown signs of affecting biodiversity and the current rate of biodiversity loss is exceeding the natural rate of extinction. All of these are important issues of environmental sustainability because they have implications for how the natural environment remains productively stable and resilient to support human life and development.

SELF-ASSESSMENT EXERCISE

i. List the three pillars of sustainable development and explain two

3.3 The Sustainable Development Goals (SDGs)

There has always been global concerns for the judicious use of available resources. The latest of such concerns was the Millennium Development Goals (MDGs) and the Sustainable Development Goals (SDGs). However, in spite of the relative effectiveness of the MDGs, not all the targets of the eight goals were achieved hence, the introduction of the SDGs to continue with the development agenda. The MDGs resulted into the SDGsafter being rolled out from 2000 to 2015.

During the 2015 United Nations Sustainable Development Summit, world leaders adopted the 2030 Sustainable Development Agenda, with 17 Sustainable Development

Goals (SDGs) which is aimed at ending poverty, fighting inequality and injustice and tackling climate change by 2030. The 17 SDGs all accompanied by 169 specific targets are listed below:

1. End poverty in all its forms everywhere.
2. End hunger, achieve food security and improved nutrition and promote sustainable agriculture.
3. Ensure healthy lives and promote well-being for all at all ages.
4. Ensure inclusive and equitable quality education and promote lifelong learning opportunities for all.
5. Achieve gender equality and empower all women and girls.
6. Ensure availability and sustainable management of water and sanitation for all.
7. Ensure access to affordable, reliable, sustainable and modern energy for all.
8. Promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all.
9. Build resilient infrastructure, promote inclusive and sustainable industrialization and foster innovation.
10. Reduce inequality within and among countries.
11. Make cities and human settlements inclusive, safe, resilient and sustainable.
12. Ensure sustainable consumption and production patterns.
13. Take urgent action to combat climate change and its impacts.
14. Conserve and sustainably use the oceans, seas and marine resources for sustainable development.
15. Protect, restore and promote sustainable use of terrestrial ecosystems, sustainably manage forests, combat desertification, and halt and reverse land degradation and halt biodiversity loss.
16. Promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels.

17. Strengthen the means of implementation and revitalize the global partnership for sustainable development

Agenda 2030 has five overarching themes, known as the five Ps: people, planet, prosperity, peace and partnership as shown in Figure 5.

Figure 5: The five themes of sustainable development

Source: www.iynf.org

SELF-ASSESSMENT EXERCISE

i. List and explain some of the sustainable development goals.

ii. What are the five themes of sustainable development?

3.4 Policies for Achieving Sustainable Development

The following are the policies for achieving sustainable development. Please note that they are by no means exhaustive.

1. Reducing Poverty:- The foremost policy is to reduce poverty. The projects with greater employment opportunities for the poor should be started. Investments in social amenities such as supply of drinking water, sanitation facilities etc., will improve environmental quality.

2. Removal of Subsidies: - To reduce environmental damages, the subsidies given for use of resources such as electricity, fertilizers, pesticides and diesel, etc., should be removed. These subsidies lead to their wasteful use. They also generate environmental problems.

3. Market Based Approaches: - There is urgent need for adopting market based approaches for the protection of environment. They aim at pointing to the consumer and industries about the cost of using natural resources on the environment. These instruments are in the form of environmental taxes which include pollution charges and user charges. The market based instruments approach is the best policy.

4. Economic Incentives: - Economic incentives regarding price, quantity and technology can also help. Incentives are usually given in the form of variable fees to resource users for the quantity of pollutants in air, water and land use. They are given rebates if less waste or pollution is generated than the standards laid down by the government.

5. Public Awareness: - Public awareness and participation are quite effective to improve environmental conditions. Formal and informal education programmes relating to environment management should be conducted. Public participation can render useful assistance in afforestation, conservation of wildlife, management of parks, etc.

6. Participation in Global Environmental Efforts: - It is felt that participation in global environmental efforts can help to minimise damages made by degradation of the environment. There should be agreements on environmental protection.

7. Trade Policy: - Trade policy stresses on the establishment of less polluting industries away from the cities and the use of environmental friendly processes for polluting industries by adopting cleaner technologies.

SELF-ASSESSMENT EXERCISE

i. Discuss the policies necessary for achieving sustainable development.

4.0 CONCLUSION

Sustainable development has attracted much attention in the governance, planning and development intervention space. It has been embraced as an appropriate development

paradigm because most of the challenges confronting humankind today such as climate change, depletion of ozone layer, water scarcity, loss of vegetation, inequality, insecurity, hunger, deprivation and poverty; can be addressed by adhering to the tenets of sustainable development. It can be argued that, sustainable development aims at achieving social progress, environmental protection and economic growth.

5.0. SUMMARY

In this unit, we discussed the meaning of sustainable development as outlined by the United Nations. The relationship among the three pillars – economic, social and environmental sustainability were also discussed as ultimate aim of sustainability. We also discussed the policies for achieving sustainable development knowing fully well that in order to translate concept into action, public participation must be encouraged.

6.0 TUTOR-MARKED ASSIGNMENT

(i) Define the concept of sustainable development and explain.

(ii) What are the goals of sustainable development?

(iii) Use a diagram to illustrate the relationship between the social, environmental, economic sustainability.

(iv) What policies would you recommend to aid in achieving the SDGs in Nigeria?

7.0 REFERENCES/FURTHER READINGS

Brodhag, C., & Taliere, S. (2006). Sustainable development strategies: Tools for policy coherence. *Natural Resources Forum*, 30, 136–145. doi:10.1111/narf.2006.30.issue-2

Daly, H. E. (1992). United Nations conference on environment and development: Retrospect on Stockholm and prospects for Rio. *Ecological Economics: the Journal of the International Society for Ecological Economics*, 5, 9–14. www.doi:10.1016/0921-8009(92)90018-N

United Nations Conference on the Human Environment. (1992). Rio Declaration on Environment and Development. Rio de Janiero, Brazil: United Nations.

Diesendorf, M. (2000). Sustainability and sustainable development. In D. Dunphy, J. Benveniste, A. Griffiths, & P. Sutton (Eds.), *Sustainability: The corporate challenge of the 21st century* (pp. 2, 19–37). Sydney: Allen & Unwin

Mensah, J. (2019). *Sustainable development: Meaning, history, principles, pillars, and implications for human action: Literature review.* Retrieved from https://www.tandfonline.com/doi/citedby/10.1080/23311886.2019.1653531?scroll=top&needAccess=true

www.sustainabledevelopment.org

MODULE TWO: SELECTED THEORIES OF ECONOMIC GROWTH AND DEVELOPMENT

Unit 1 Structural-Change Growth Theory
Unit 2 International-Dependence Theories
Unit 3 Neoclassical Growth Model
Unit 4 Endogenous Growth Model and Policy Implications

UNIT 1: THE STRUCTURAL-CHANGEGROWTH THEORY

CONTENTS

1.0 Introduction
2.0 Objectives
3.0 Main Content
- 3.1 Explanation of the Lewis Growth Theory
- 3.2 Basic Assumptions of the Model
- 3.3 The Criticisms of the Model
- 3.4 The Relevance of the Model to Developing Economies.

4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References/Further Readings

1.0 INTRODUCTION

The structural-change theory focuses on the mechanism by which underdeveloped economies transform from heavy emphasis on traditional subsistence agricultural to a more industrialised economy. A well-known representative example of the structural change theory is the Lewis dual sector theory which was developed by Arthur Lewis. The theory underscored the importance of the surplus labour inherent in underdeveloped economies, hence, it became the general theory of development process for surplus labour nations during 1960s and early 1970s. In this unit, we examine the Lewis theory of development.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

i. Explain the Lewis development theory
ii. Highlight the assumptions of the model

iii. Give a critical evaluation of the model

iv. Discuss the relevance of the model to a developing economy.

3.0 MAIN CONTENT

3.1 The Lewis Two-Sector Surplus-Labour Model of Development

Lewis theory of economic development is a structural change theory. This theory explains the mechanism of changing structure of underdeveloped economics from subsistence agriculture to more a modern and more urbanized economy (Onwuka, 2011). The Lewis model consists of two sectors: A traditional, rural subsistent sector characterized by zero marginal labour productivity and a high productivity modern urban industrial sector into which the surplus labour from the traditional sector is transferred. The theory argues that as labour leaves the agricultural sector to industries, the MPL in the latter would increase and push up income in the sector because the population has the potential of expanding the domestic market for industrial goods.

Lewis model consists of two sectors in the economy. They are

i) Traditional sector which is the overpopulated subsistence sector where marginal productivity of labour is zero. Due to zero marginal productivity of labour it is possible to withdraw labour from this sector without affecting the level of output. This is why Lewis classified this sector as surplus labour sector.

ii) Modern sector which is the urban industrial sector. Productivity is high in this sector. Labour is gradually transferred from the traditional sectorinto this sector. Movement of labour from traditional to modern sector brings the expansion in both output and employment. The speed of this expansion depends on:

   a) The rate of industrial investment and capital accumulation which ultimately depends on the level of profit. Lewis assumes that all profits are re-invested.

b) Wage differential between the rural and the urban sectors. According to Lewis there should be at least 30% higher wage rates in the urban sector than in the rural sector in order to transfer labour automatically from rural to urban sector. Lewis assumed that there is perfectly competitive labour market in modern sector giving fix wage rate and horizontal supply curve of labour. On the other hand wage rate in the traditional sector is given by average productivity of labour($w = APP_L = TP/L$)

We can explain Lewis model in two sector economy with the help of Figure 7.

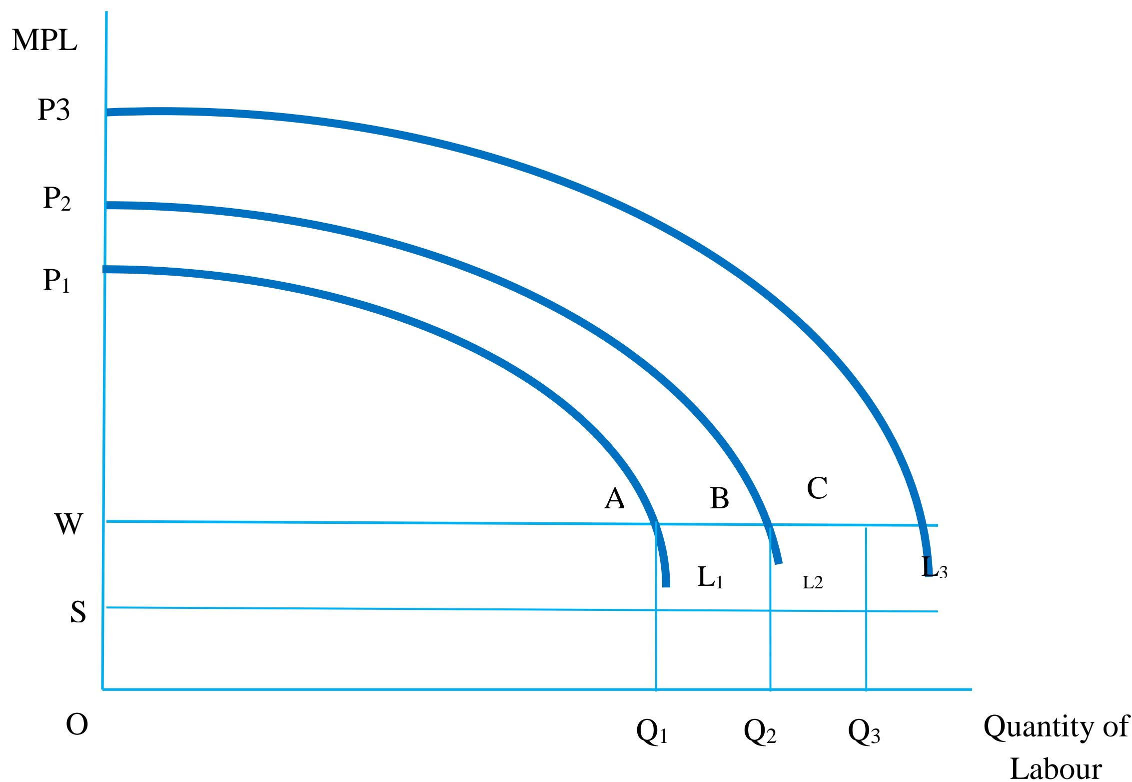

Figure 7: Graphical representation of the Lewis model

Source: Ahuja (2016)

In Fig 7, line *OS* represents the agricultural (traditional) sector labour wage which is less than the industrial sector wage represented by the distance *OW*. Traditional sector production depends on labour (variable factor) and capital and technology (fixed factors).

The labour supply curve which is W is elastic. This means that at OW wage in the industrial sector, the supply of labour is unlimited. At the stage when OQ_1 of labour is employed in the industrial sector, the MP curve is P_1L_1 and the total output of the sector is OP_1AQ_1. Out of this, workers are paid $OWAQ_1$ leaving the area WP_1A as surplus output or the capitalist surplus or total profit earned by the industrial sector, resulting from labour drawn from the traditional sector.

When the surplus is reinvested, the MP curve shifts upwards to P_2L_2 and the capitalist surplus and the employment are larger than before, from WP_1A to WP_2B and OQ_1 to OQ_2respectively. Further reinvestment as expected in the industrial sector further raises both the MP curve and the level of employment to P_3L_3 and OQ_3. This continues until the entire surplus labour is absorbed in the capitalist or industrial sector, including mining and so on. As the economy continues to develop, wages and employment would continue to rise. The increased profit is again reinvested. This process continues giving a self-sustained growth until the surplus labor is absorbed in the new industrial sector. When all the surplus labour in the subsistence sector has been attracted into the capitalist sector, wages in the subsistence sector will begin to rise, shifting the terms of trade in favour of agriculture and causing wages in the capitalist sector to rise.

SELF-ASSESSMENT EXERCISE

i. Explain the structural-change theory.

ii. Use a graph to explain the Lewis surplus labour theory

3.2. Some Assumptions of the Theory and the Evaluation

3.2.1 Some Assumptions of the Theory

1. Wage rate in the industrial sector is fixed and higher than what is obtainable in the industrial sector. This differential is able to pull labour out from the subsistence sector.

2. Lewis assumes absence of unemployment in the industrial sector while disguised unemployment prevails in the subsistence sector.

3. Labour is perfectly mobile especially from the agricultural sector to the industrial sector and the movement of labour from the agricultural sector to the industrial sector has no effect on the volume of production in the agricultural sector.

4. Marginal product of labour is assumed to be zero or even negative in the subsistence sector.

5. Employment in the modern sector is made possible by the existence of output expansion, which is a bye-product of capital accumulation, and capital accumulation is the result of excess profits over wages in the industrial production system.

3.2.1 Evaluation of the Model

In evaluating the labour surplus development theory, it is pertinent to point out that wage rates can never be constant in real life situation even in the face of adverse economic situations. The model is therefore, misleading by its neglect of time differential and dimension (Jhingan, 2011). For example in developing countries, wage rates continues to rise in the industrial sector over time even when there is open unemployment in the rural sector. Moreover, in a situation where the productive capital is labour saving, it would be absurd to expect it to absorb labour as the theory asserts.

This logic of labour being absorbed in the productive sector and paid the same wage is inconsistent with the economic reality as the following diagram depicts.

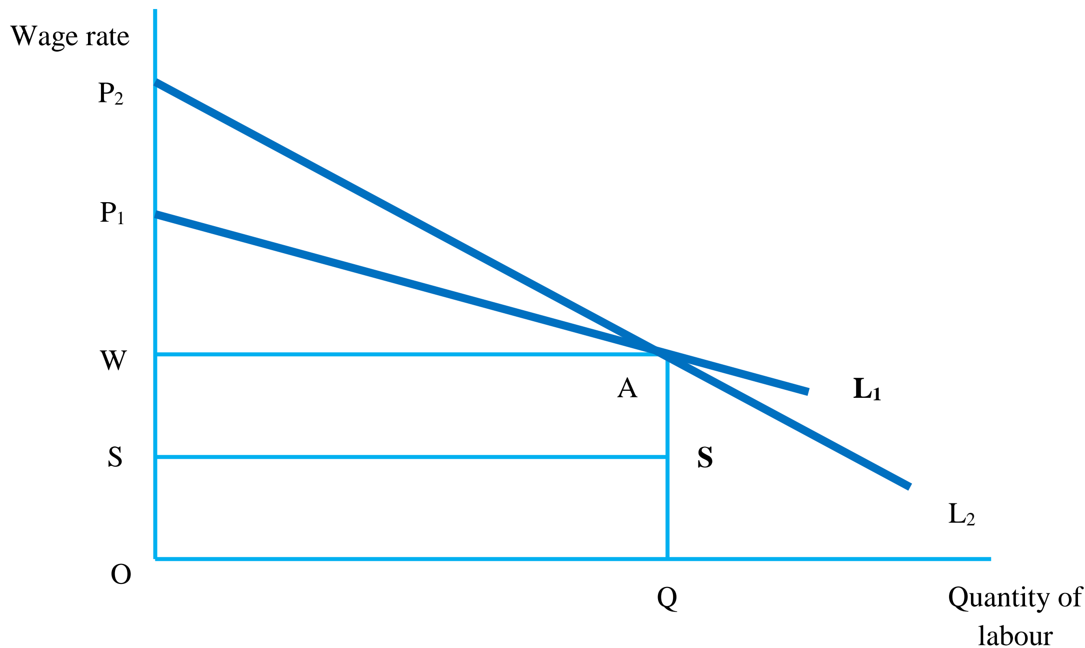

Figure 8: Labour-saving capital accumulation:Employment implication
Source: Ahuja (2016)

Figure 8 shows that the curve P_2L_2 has a greater negative slope than the P_1L_1curve indicating the use of labour saving technique. The MP_L curve shifts upward from P_1L_1 to P_2L_2 raising the total output from OP_1AQ to OP_2AQ despite the total wage bill *OWAQ* and the labour employed remaining unaltered at *OQ*.

Secondly, the theory fails to consider the possibility of progress in the agricultural sector. But from all available evidence, there is considerable progress in the long run in this sector. This ensures that labour is not as mobile as the theory assumes based on several factors, such as family size, acquired skill, religion, language, culture and so on.

Thirdly, if the MP_L in the underdeveloped country is zero as the theory assumes, the subsistence wage would also be zero. This means that productivity would fall with migration of labour from the subsistence sector to the industrial sector as against the assumption of the theory.

Fourth, Evidence in developing countries shows that surplus labour is as likely in the urban sectors as is in the rural agricultural sectors because migrating workers may have limited information concerning job availability, payment and working conditions and this results in unemployment in cities. Also towns and cities may not be able to accommodate

large numbers of immigrant workers and this gives rise to slums and shanty towns as well as other eco problems

All this notwithstanding, the theory is an important step forward in the attempt to formulate, define and elaborate on the economic problems facing the developing countries.

SELF-ASSESSMENT EXERCISE

i. Identify three major assumptions of the surplus labour theory.
ii. Evaluate the assumptions of the surplus labour theory.

4.0 CONCLUSION

The Lewis model is a model of structural change because it outlines the development from a traditional economy to an industrialized one. It is a labour-surplus theory because Lewis argued that there is surplus labour in the rural subsistence agricultural sector. The theory assumes that marginal productivity of labour in the agricultural sector is zero or negligible. But one of the flaws in the Lewis two-sector model is that the theory failed to recognize the possibility of progress in the agriculture sector. The progress in the agricultural sector will make it difficult for labour to migrate to the urban area. But despite the criticism, the theory is able to explain one of the major economic problems facing the developing countries.

5.0 SUMMARY

The features of the Lewis surplus labour theory was extensively discussed with the aid of a diagram. We also discussed the assumptions of the model as well as the criticisms of the model. We conclude that the two-sector surplus-labour theory is relevant in analyzing the economic problems in developing countries.

6.0 TUTOR MARKED ASSIGNMENTS

i. With the aid of well- labeled graph, discuss the features of the Lewis two-sector theory.

ii. Discuss the basic assumptions of the surplus- labour theory

iii. Do you think Lewis model is relevant to the Nigerian economy? Justify your answer**.**

7.0 REFERENCES/FURTHER READING

Ahuja, H. L. (2016). *Development economics*. New Delhi: S. D. Chand.

Jhingan, M.L. (2011). The economics of development and planning, *40th edition*. Indis: Vrinda Publications

Onwuka, C. E. (2011). *Economic development monograph series 3*. Ekpoma: Pon Publishers

Todaro, M. P. & Smith, S. C. (2012). *Economic development*. *11th edition*. USA: Pearson Publishers.

Zarra-Nezhad, M. & Hosainpour, F. (2011). Review of growth models in less developed countries. *The International Journal of Applied Economics and Finance, 5*(1), 1-7.

UNIT 2: INTERNATIONAL-DEPENDENCE THEORY

1.0 Introduction
2.0 Objectives
3.0 Main Content
    3.1 The Meaning of International Dependence Theory
    3.2 The Sub Groups of the Dependence Theory
    3.3 The Major Weaknesses of the Dependence Theory.
    3.4 The Policy Implications of the Dependence Theory
4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References/Further Readings

1.0 INTRODUCTION

The inability of the existing theories of growth to bring about changes in developing countries, led the developing countries economists to develop new theories of development. These theories came to be identified as the International-Dependence Theories. This school of thought argues that the main cause of underdevelopment is the result of over dependence of developing countries on the developed countries. The scholars believe that the developing countries are caught up in a dependence and dominance relationship with the developed countries. In this unit, we will discuss the different strands of the international-dependence theory, the major weaknesses and policy implications of the dependence theory.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

i. Explain the international dependence theory of underdevelopment.
ii. Discuss the sub groups of the dependence theory.
iii. Narrate the major weaknesses of the dependence theory.
iv. Outline the policy implications of the dependence theory

3.0 MAIN CONTENT

3.1.1 The International Dependence Theory of Underdevelopment

The international-dependence theory, an approach to understanding economic underdevelopment that emphasizes the supposed constraints imposed by global and

political economic order. It was proposed in the 1950s by Raul Prebish and gained prominence in the 1960s and 1970s. The principal idea behind the international-dependence theory is that the underdeveloped countries are caught up in a dependence and dominance relationship with the rich countries (Onwuka, 2011). The rich developed countries either intentionally or unintentionally encourages this unequal relationship (Jhingan, 2011). According to the theorists in this school of thought, the world is divided into two groups: The center and the periphery. The center is the developed countries such as Britain, USA, European countries, etc.; while the periphery is the less developed countries such as African countries, Latin American and other backward Asian countries. The center is the dominant while the periphery is dependent on the center in an unequal relationship in trade activities, technology, investment, and so on. This dependency results in underdevelopment of the periphery due to exploitation by the capitalist countries who are powerful in global economic activities (Onwuka, 2011).

According to Dos Santos (1971), dependence is when some countries condition their economy by the development and expansion of another country to which the former is subjected to and this can be beneficial or detrimental to their instant development.

Dependence theory found the causes for the lack of development to be external to the socioeconomic formations of the less developed countries (LDCs). It does not treat the dysfunctional institutions of the LDCs as the cause of backwardness. Internal institutional structures such as corruption levels, unproductive land holdings, concentration of wealth, and unresponsive political systems are never considered the causes of underdevelopment (Egyankosh, n.d). Many dependency theorists advocate social revolution as an effective means to reduce economic disparities in the world system.

3.1.2 The basic premises of the international -dependence theory are:

i). The periphery are disadvantaged in their interactions with the center. They provide natural resources and cheap labor and serve as export destinations for obsolete

technology as well as for markets for the developed countries (center), without which, the latter could not have the standard of living they enjoy.

ii). The developed and wealthy nations actively perpetuate a state of dependence through various means such as economic control, media control, politics, banking and finance, education, culture, sport, and all aspects of human resource development, including the recruitment and training of workers

iii) The wealthy nations actively counter all attempts made by dependent nations to resist their influences by means of economic sanctions, and, possibly, by the use of military force. The poverty of the countries in the periphery is not because they are not integrated into the world system, or not fully integrated as is often argued by free market economists, but because of how they are integrated into the system.

SELF-ASSESSMENT EXERCISES

(i). Discuss the arguments of international-dependence theory.

(ii). What are the basic premises of international- dependence theory?

3.2 The Sub Groups of the International-Dependence Theory

The ideas that developed under the broad heading of international-dependence theory can be further classified into the following three sub groups.

a). The Neocolonial Dependence Model: This is an indirect outgrowth of Marxist thinking (Munro, 2018). According to this doctrine, underdevelopment is viewed as the result of highly unequal international capitalist system or what is called the rich country-poor country relationships. The rich developed countries through their intentionally exploitative or unintentionally neglectful policies hurt the developing countries. Then using a small elite ruling class in the developing countries, they serve as agents to the rich countries, and perpetuate underdevelopment in the developing countries. These basic attributes of dependence lead to backwardness, exploitation and impoverishment.

Unlike other development models that believe that underdevelopment is a result of internal constraints such as insufficient savings, investment or lack of infrastructure, skill or education; the proponents of the neocolonial dependence model believe that underdevelopment is an externally induced phenomenon (Munro, 2018). According to the advocates of this idea, the remedy was to initiate revolutionary struggles that will topple the existing elite of the developing countries. The also emphasized on the need to restructure the world capitalist system so as to free developing nations from the unholy control of their domestic oppressors.

b). The False Paradigm Model: The false paradigm advocates believe that although the developed countries may have good intentions of helping the developing countries, but their expert policy advises from their countries and agencies such as World Bank and International Monetary Fund are simply inappropriate in the context of developing countries (Todaro & Smith, 2015). The experts offer sophisticated concepts with elegant theoretical and econometric models without incorporating the unique social, cultural and institutional characteristics of the developing countries. As a result, the policies become inhibitive to and out of tune with the development aspirations of the developing countries.

c). The Dualistic-Development Thesis: Dualism simple means the relationship between the rich and the poor countries in an international and domestic activities. Domestic dualism is the coexistence of an advanced imported capitalist system and an indigenous pre-capitalist backward system. Domestic dualism is characterized by the existence of modern relatively developing sector producing primary products for export on one side and an isolated subsistence-based underdeveloped sector on the other side (Metu et al., 2017).

Dualism leads to the dominance of the center and the dependence of the periphery by encouraging the flow of foreign investment into developing countries, encouraging the exportation of primary products by developing countries, by controlling natural resources in developing countries, etc.

The interrelations between the superior and inferior elements are such, be it in a global sense or in a local sense, that the superior elements do little or nothing to pull up the inferior element. In fact, the developed countries may push down the underdeveloped regions with the result that there is entrenchment of underdevelopment (Jhingan, 2011). The dependency theory emphasized on international power imbalances and on needed fundamental economic, institutional, political reforms. In extreme cases, they advocate for an outright expropriation of privately owned assets believing that public asset ownership and control will be more efficient and effective in delivering development (Ahuja, 2016).

SELF-ASSESSMENT EXERCISE

i. What is the argument of the false paradigm model?
ii. Discuss the arguments of the dualistic development thesis

3.3 Major Weaknesses of International-Dependence Theory

The International-Dependence theory suffers from some weaknesses and they are:

(i) The theory focuses mainly on the reasons for continuous underdevelopment in developing countries. They lack any concrete ideas as to how a country should initiate and sustain development. The theory helps in understanding what is causing the underdeveloped countries to remain underdeveloped but do not give the clue regarding how the country should come out of such a situation.

(ii) The explanation of underdevelopment by the dependency theorists can be said to be one sided because they explained underdevelopment as an exchange or trade relations between the center and the periphery (Onwuka, 2011). They ignored the problems of forces of production and relations of productions in the developing countries. It failed to explain how the surplus that is to be exchanged is produced and appropriated in the developing countries.

(iii) Some dependency economists believe that foreign investment by multinational corporations is exploitative by way of capital flight, but they ignore the contributions of these multinational corporations in developing countries. They contribute to production and export by re-investing their profit in the domestic economy.

(iv) The critics argue that the characteristics of dependence are not well defined by the theorists because the characteristics of dependence found in developing countries are also found in non-dependent countries. For instance, the dominance of foreign capital is a characteristics of capitalist development and does not provide a criterion of dependence.

(v) Large scale failure of countries which followed the more radical approach and took the revolutionary path. These countries overthrew their existing elite and pursued revolutionary campaign of industrial nationalization but at the end failed to attain any significant improvement in people's standard of living.

(vi) Reyes (2001) suggest that the dependency analysis was unable to prove its basic thesis scientifically and could not show that dependency and development were incompatible.

SELF-ASSESSMENT EXERCISE

i. Expose the weaknesses found in the international-dependence theory of underdevelopment.

3.4 Policy Implications of the International-Dependence Theory

i) The dependence theory advocates that developing countries can adopt new development strategy that involves a policy of self-reliance. In pursing self-reliance, they should endorse interactions with the rest of the world in the areas which improve the social and economic welfare of the larger economy.

ii) International-dependence theorists suggest that to overcome dependence, developing countries should engage in internal institutional and structural changes in all the sectors of the economy (Jhingan, 2011). There should be agricultural reform so as to increase

supply of farm products at a lower prices and increase productivity. This will create surplus export and help to reduce foreign dependence.

iii) Dependency theorists do not deny that economic activity occurs within a dependent state, they rather make a very important distinction, between economic growth and economic development. For example, there is a greater concern within the dependency framework for whether the economic activity is actually benefitting the nation as a whole. Therefore, far greater attention is paid to indices such as life expectancy, literacy, infant mortality, education, and the like. Dependency theorists clearly emphasize social indicators far more than economic indicators.

iv). Dependent states, therefore, should attempt to pursue policies of self-reliance. Contrary to the neo-classical models endorsed by the International Monetary Fund and the World Bank, greater integration into the global economy is not necessarily a good choice for poor countries. Often this policy perspective is viewed as an endorsement of a policy of autarky, and there have been some experiments with such a policy such as China's Great Leap Forward or Tanzania's policy of *Ujamaa*. The failures of these policies are clear, and the failures suggest that autarky is not a good choice. Rather a policy of self-reliance should be interpreted as endorsing a policy of controlled interactions with the world economy. Poor countries should only endorse interactions on terms that promise to improve the social and economic welfare of the larger citizenry.

SELF-ASSESSMENT EXERCISE

i. Discuss the policy implications of the international-dependence theories.

4.0 CONCLUSION

The international-dependence theories contend that resources flow from a periphery of poor underdeveloped economies to the center called the developed economies, thereby enriching the center at the expense of the periphery. Dependency theorists argue that underdeveloped countries should be self-reliant in pursuing their growth path.

5.0 SUMMARY

We studied about the meaning, and major streams of thoughts of the international-dependence theories. We also discussed the criticisms levied against the various strands of the models. Finally, we discussed the policy implications of the international-dependence theories

6.0 TUTOR-MARKED ASSIGNMENTS

i. Explain the international-dependence theories of development highlighting the basic premise of the theory.

ii. Identify the major streams of thought of the international-dependence theories and their individual arguments.

iii. Narrate the criticisms leveled against the international-dependence theories.

iv. How relevant is the international-dependence theory in the explanation of underdevelopment in Africa and Latin America.

7.0 REFERENCES/FURTHER READINGS

Ahuja, H. L. (1980). *Modern economics*. New Delhi: S. D. Chand.

Ahuja, H. L. (2016). *Development economics*. New Delhi: S. D. Chand.

Amin, S. (1976). *Unequal development: An essay on the social formations of peripheral capitalism*. New York: Monthly Review Press.

Cardoso, F.H. & Enzo, F. (1979). *Dependency and development in Latin America*. Berkeley CA: California University Press.

Dos Santos, J. (1971). The structure of dependence. In K. T. Fann and D. L. Hudges (eds). *Readings in US imperialism*. Boston: Porter Satgent.

Munro, A. (2018). Dependency theory. Britannica. Retrieved from www.britannica.com

Onwuka, C. E. (2011). *Economic development monograph series 3*.Ekpoma: Pon Publishers

Todaro, M. P. & Smith, S. C. (2012). *Economic development, 11th Edition*. USA: Pearson Publishers.

http://www.egyankosh.ac.in/bitstream/123456789/8981/1/Unit-3.pdf

UNIT 3 NEOCLASSICAL GROWTH THEORY

1.0 Introduction
2.0 Objectives
3.0 Main Content
  3.1 Neoclassical Growth Model
  3.2 Assumptions of the Model
  3.3 Key Implications of the Model
4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
8.0 References/Further Readings

1.0 INTRODUCTION

The neoclassical growth theory was developed in the 1956 in the field of growth economics. Two prominent contributors to the theory are Robert Solow and Trevor Swan. The model first considered exogenous population increases to set up growth rate, but in 1957, Solow incorporated technology change into the model. Hence, the neoclassical theory emphasizes capital accumulation as the main determinant of economic growth. In this unit, we will discuss the main thesis of the theory, the assumptions of the model and the practical importance of the model to developing countries.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

i. Discuss the neoclassical growth model.
ii. Highlight the assumptions of the model.
iii. Explain implications of the model to developing countries.

3.0 MAIN CONTENT

3.1 The Neoclassical Growth Theory

The Neoclassical Growth Theory is an economic model of growth that outlines how a steady economic growth rate results when three economic forces - labor, capital, and technology, come into play. The simplest and most popular version of the neoclassical growth model is the Solow-Swan model.

The Solow-Swan model is an economic growth model explaining the long-run economic growth within the neoclassical economies. It explains how long-term economic equilibrium is as a result of the role played by varying amounts of labour or population growth and capital in the process of production. It also added technology as an exogenously determined factor in the production function. Hence, the theory argues that technological change significantly influences the overall functioning of an economy. The neoclassical growth model claims that capital accumulation and how it is used in an economy, is important for determining economic growth.

The Assumptions of the Neoclassical Growth Model

(i). An important assumption of the neoclassical growth model is that capital (K) is subject to diminishing returns provided the economy is a closed economy.

(ii). In the short term, the rate of growth slows down as diminishing returns take effect, and the economy converts into a "steady-state" economy, where the economy is steady, or in other words, in a relatively constant state.

(iii). Provided that labor is fixed or constant, the impact on the total output of the last unit of the capital accumulated will always be less than the one before.

SELF-ASSESSMENT EXERCISES

- **i.** Explain the neoclassical growth theory
- **ii.** What are the basic assumptions of the neoclassical growth theory?

3.2 The Neoclassical Growth Theory and the Production Function

Given these assumption, the neoclassical growth model is built on the production function showing the relationship between capital, labour and productivity in an economy. Therefore, the production function of the neoclassical growth model is used to measure the economic growth and equilibrium of an economy. The Solow model is set in

continuous-time world with no government or international trade. The general production function in the neoclassical growth model takes the following Cobb-Douglas form:

$$Y(t) = K(t)^{\alpha} \{ A(t) L(t)\}^{1-\alpha} \quad (1)$$

Where: ***Y****(t)* is total production or gross domestic product (GDP) or income of the economy, ***K*** is capital stock, ***L*** is the amount of labour in the economy and ***A*** is the exogenously determined level of technology or knowledge, thus ***AL*** represents effective labour. $0 < \alpha < 1$ is the elasticity of output with respect to capital. Due to constant returns to scale, if all inputs are increased by the same amount, say 10%, then output will increase by the same amount (10% in this case).

From Cobb-Douglas function in Equation (1)

$$Y(t)= Ak(t)^{\alpha} \quad (2)$$

Equation 2 states that output per worker is a function that depends on the amount of capital
per worker. The more capital with which each worker has to work, the more output that worker can produce.

$$y(t)= \frac{Y(t)}{A(t)L(t)} = k(t)^{\alpha} \quad (3)$$

The main interest of the model is the dynamics of capital intensity K, the capital stock per unit of effective labour. Its behaviour over time is given by the key equation of the Solow–Swan model.

$$K(t)= sk(t)^{\alpha} - (n + g + d) K(t) \quad (4)$$

Where s, n and g are saving rate, population growth rate, and the technological change rate, respectively. The equation implies that $K(t)$ converges to a steady-state value of K^*, defined by $sk(t)^{\alpha} = (n + g + d) K(t)$, at which there is neither an increase nor a decrease of capital intensity. The first term, $sk(t)^{\alpha}$, is the actual investment per unit of effective labour while the second term, $(n + g + d) K(t)$, is the “break-even investment”.

$$K* = \left(\frac{s}{n+g+d}\right)^{\frac{1}{1-\alpha}} \quad (5)$$

In essence, the Solow–Swan model predicts that an economy will eventually converge to a balanced-growth equilibrium. In this situation, the growth of output per worker is determined solely by the rate of technological progress. Therefore, at the equilibrium, the capital/output ratio depends only on the saving, growth, and depreciation rates. This is the Solow–Swan model's version of the golden rule saving rate. A nation that devotes a large fraction of its income to savings will have a higher steady-state capital stock and a high level of income.

Unlike the Harrod-Domar growth model that uses fixed production function, the neoclassical growth model uses variable proportion production function, that is, it considers unlimited possibilities of substitution between labour and capital. Also, another departure from the Harrod-Domar model is that the neoclassical model assumes equality between savings and investment due to adjustments in price. Similarly, the neoclassical growth model does not consider aggregate demand as limiting economic growth but rather focuses on the supply side factors such as capital and technology as determining economic growth in an economy. The growth of output in this model is achieved at least through higher rate of saving and therefore higher rate of capital formation. However, diminishing returns to capital limit economic growth in this model. Though the neoclassical growth model assumes constant return to scale which exhibits diminishing returns to labour and capital.

Key Conclusions of the Neoclassical Growth Model

- **Long-term growth rate**: The long-term growth rate of an economy is solely determined by technological progress or regress.
- **Output as a function of growth**: The neoclassical growth model explicates that total output is a function of economic growth in factor inputs, capital, labor, and technological progress.

- **Growth rate of output in a steady-state equilibrium**: The growth rate of total output in a steady-state equilibrium is equal to the growth rate of the population or labor force and is never influenced by the rate of savings.
- **Increased steady-state per capita income level**: While the rate of savings does not influence the steady-state economy growth rate of total output, it does result in an increase in the steady-state level of per capita income and, therefore, total income as well, as it raises the total capital per head.

SELF-ASSESSMENT EXERCISES

i. Explain the Solow-Swan growth theory.

ii. Identify three key conclusions of the Solow-Swan theory?

3.3 Implications of the Solow-Swan Model

(i). If the saving rate increases, it increases the output per worker by increasing the capital per worker, but the growth rate of output is not affected.

(ii). Secondly, the implication of the model is that growth in per capita income can either be achieved by increased saving or reduced rate of population growth. This will hold if depreciation is allowed in the model.

(iii). Third according to the model, in the absence of continuing improvements in technology, growth per worker must ultimately cease. This prediction follows from the assumption of diminishing returns to capital.

(iv). Fourth the model predicts conditional convergence. All countries having similar characteristics like saving rate, population growth rate, technology, etc. that affect growth will converge to the same steady state level. It means that poor countries having the same saving rate and level of technology of the rich countries will reach the same steady state growth rates in the long run.

SELF-ASSESSMENT EXERCISE

i. Explain at least three implications of the Solow-Swan growth theory.

4.0 CONCLUSION

The Solow-Swan growth theory was developed in 1956. The Solow-Swan model of economic growth postulates a continuous production function linking output to the inputs of capital and labour which leads to the steady state equilibrium of the economy. Using the Cobb-Douglas production function, technology is thought to augment labour productivity and increase the output capabilities of labour.

5.0 SUMMARY

This unit discussed the neoclassical growth theory as developed by Solow-Swan in 1956 and its contribution to modern growth theory. We also discussed the assumptions of the growth model. One of the fundamental feature of this model is its competitive framework and its assumption of constant returns to scale and diminishing returns.

6.0 TUTOR-MARKED ASSIGNMENTS

i. Explain the neoclassical growth model using the production function
ii. Outline the main contributions of the neoclassical growth model to development discourse.
iii. How applicable is the neoclassical growth model to the Nigerian economy.

7.0 REFERENCES/FURTHER READINGS

Ahuja, H. L. (2016). *Modern economics*. New Delhi: S. D. Chand.

Jhingan, M.L. (2011). *The economics of development and planning, 40th edition*. Indis: Vrinda Publications.

Masoud, N. (2013). Neoclassical economic growth theory: An empirical approach. *Far East Journal of Psychology and Business, 2*(3), 10-33

Zarra-Nezhad, M. & Hosainpour, F. (2011). Review of growth models in less developed countries. *The International Journal of Applied Economics and Finance, 5*(1), 1-7.

Todaro, M. P. & Smith, S. C. (2012). *Economic development,11th Edition*. USA: Pearson Publishers.

UNIT 4 THE ENDOGENOUS GROWTH MODEL AND POLICY IMPLICATIONS

1.0 Introduction
2.0 Objectives
3.0. Main Content
3.1. The Main Features of the Endogenous Growth Theory
3.2. The Assumptions and Criticisms of the Endogenous Growth Theory
3.3. The Policy Implications of Endogenous Growth Theory.
4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References/Further Readings

1.0 INTRODUCTION

The endogenous growth theory was developed by economists including Arrow, Paul Romer and Robert Lucas in the mid-1980s. The theory came about as a reaction to the deficiencies and omissions in the Solow-Swan neoclassical growth model. It is also called new growth theory and it explains the long-run growth rate of an economy on the basis of endogenous factors as against exogenous factors of the neoclassical growth theory. In this unit, we briefly study the main features of the endogenous growth theory, criticisms and policy implications.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

i. Discuss the main features of the endogenous growth theory
ii. Enumerate the criticisms against the theory
iii. Outline the policy implications of the theory.

3.0 MAIN CONTENT

3.1 Features of the Endogenous Growth Models

The endogenous growth theory states that economic growth is generated internally in the economy, i.e., through endogenous forces, and not through exogenous ones as the

neoclassical growth model suggests (Ahuja, 2016). The endogenous growth theory argues that technological progress which is the main source of economic growth is a response to economic incentives in the market that can be influenced by the government or the private sector. Endogenous growth theory states that investment in human capital, innovation and knowledge are significant contributions to economic growth because they help to develop new technology and make production more efficient (Metu et al., 2017). They did not simply criticise the neoclassical growth theory. Rather, it extends the latter by introducing endogenous technical progress in growth models. The endogenous growth models were developed by Arrow, Romer and Lucas among other economists. We will examine the individual models.

(A). Arrow's Learning by Doing Model

Arrow was the first economist to introduce the concept of learning by doing in 1962 and regards it as endogenous in the growth process. His hypothesis was that at any moment of time, new capital goods incorporate all the knowledge available based on accumulated experience, but once built, their productive deficiencies cannot be changed by subsequent learning. Arrow's model in a simplified form can be written as

$$Y_i = A(K)\,F(K_i, L_i) \tag{6}$$

Where Y_i is output of firm i, K_i is the stock of capital, L_i, is the stock of labour, K is the aggregated stock of capital and A is the technology factor.

According to Arrow as cited in Ahuja (1980) if the stock of labour is held constant, growth will be stopped because socially very little is invested and produced. Therefore, Arrow did not explain that his model could lead to sustained endogenous growth.

(B). The Romer Model

Romer in his first paper on endogenous growth in 1986 presented a different opinion on Arrow's model which is known as learning by investment. He assumes creation of knowledge as a side product of investment and assumes knowledge as an input in the production function of the form:

$$Y = A(R)\, F\,(R_i, K_i, L_i) \quad (7)$$

Where Y is aggregate output; A is the public stock of knowledge from research and development (R&D); R_i is the stock of results from expenditure on research and development by firm i; and K_i and L_i are capital and labour stock of firm i respectively. He assumes the function F homogeneous of degree one in all its inputs R_i, K_i, and L_i, and treats R_i as a rival good.

Romer took three key elements in the model, namely (i) externalities, (ii) increasing returns in the production of output and (iii) diminishing returns in the production of new knowledge (Jhingan, 2011). According to Romer, a firm investing in new research technology have no exclusive right to rather it spills-over instantly across the entire economy due to the inadequacy of patent protection and increase in their production.

In Romer's model, new knowledge as a result of investment in R&D is the ultimate determinant of long-run growth (Ahuja, 2016). Research technology exhibits diminishing returns which means that investments in research technology will not double knowledge. Thus the production of goods from increased knowledge displays increasing returns and competitive equilibrium is consistent with increasing aggregate returns owing to externalities. Thus Romer takes investment in research technology as endogenous factor in terms of the acquisition of new knowledge by rational profit maximisation firms.

C. The Lucas Model:

Uzawa developed an endogenous growth model based on investment in human capital which was used by Lucas. According to Ahuja (1980) Lucas assumes that investment on education and skills leads to the production of human capital which is the crucial determinant in the growth process.

He makes a distinction between the internal effects of human capital where the individual worker undergoing training becomes more productive, and external effects which spillover and increase the productivity of capital and of other workers in the economy. It

is investment in human capital rather than physical capital that have spillover effects that increase the level of technology. Thus the output for firm i take the form

$$Y_i = A(K_i).(H_i).H^e \quad (8)$$

Where A is the technical coefficient, K_i and H_i are the inputs of physical and human capital used by firms to produce goods Y_i. The variable H is the economy's average level of human capital. The parameter e represents the strength of the external effects from human capital to each firm's productivity.

In the Lucas model, each firm faces constant returns to scale, while there are increasing returns for the whole economy. Further, learning by doing or on-the-job training and spillover effects involve human capital.

Investment in human capital (labour input) is assumed to be the source of technological progress (increase in the level of technology) and the output of the firm. In the model, technology is endogenously provided as a side effect of investment decisions by firms. Technology is treated as a public good with firms being treated as price takers just like in perfect competition.

SELF-ASSESSMENT EXERCISES

i. Explain the endogenous growth model
ii. Discuss Arrow's learning by doing model
iii. Examine Romer's growth model

3.2. The Assumptions and Criticisms of the Endogenous Growth Theory

3.2.1 The Assumptions of the Model:

The endogenous growth theory is based on the following assumptions:

i) Knowledge or technological advance is a non-rival good.
ii) There are increasing returns to scale to all factors taken together and constant returns to a single factor, at least for one.
iii) Technological advance is based on the creation of new ideas that is, what people do.

iv) Many individuals and firms have market power and earn profits from their discoveries. This assumption arises from increasing returns to scale in production that leads to imperfect competition.

These are the requirements of an endogenous growth theory on which we explained the three main models of the endogenous growth theory.

3.2.2 Criticisms of the Model

The endogenous growth theory is criticized on the following grounds:

i) The critics of endogenous growth theory believe that there is nothing new in the theory because increasing returns and endogeneity of variables were taken from the neoclassical and Kaldor's models.

ii) Fisher criticized the new growth theory for depending only on the production function and the steady state.

iii) The critics argue that the theory lays much emphasis on the role of human capital and neglects the role of institutions.

iv) The various endogenous growth theory shows no clear difference between physical capital and human capital. They did not make an explicit distinction between capital accumulation and technological progress. It lumps physical and human capital whose accumulation is studied by neoclassical theory with intellectual capital accumulated through innovation (Howitt, n.d).

SELF-ASSESSMENT EXERCISES

i. Discuss the assumptions of the endogenous growth model

ii. Enumerate the criticisms of the endogenous growth model

3.3 Key Policy Implications of Endogenous Growth Theory

The endogenous growth theory has important policy implications for developing economies:

- Governmental policies can raise an economy's growth rate if the policies are directed toward enforcing more market competition and helping stimulate innovation in products and processes.
- There are increasing returns to scale from capital investment in the "knowledge industries" of education, health, and telecommunications.
- Private sector investment in R&D is a vital source of technological progress for the economy. Hence, there should be provision for making investment in human capital and on R&D of new technology so as to increase both physical and human capital.
- There should be incentives in form of subsidy to firms that invest on research and development of new technologies.
- Endogenous growth theory envisages greater role of government in promoting resource allocation and promoting investment in order to raise rate of economic growth. The government can adequately invest in infrastructure such as power, road, communication, health and education.
- Trade openness will help developing countries gain more by drawing upon new knowledge, R&D and new technology from developed countries.

SELF-ASSESSMENT EXERCISE

i. Illustrate key policy implications of the endogenous growth theory.

4.0 CONCLUSION

The endogenous growth theory also known as the new growth theory was propounded by scholars such as Arrow, Romar and Lucas with other economists as a result of the increasing dissatisfaction with the neoclassical growth theory. Endogenous growth theory argues that economic growth is as a result of endogenous efforts rather than external effort. The theory states that investment in human capital, innovation and knowledge are necessary for the growth process. The endogenous growth theory emphasizes on the need

for developing countries to invest in research and development because spill over from research efforts by one firm leads to the creation of new knowledge by other firms.

5.0 SUMMARY

We studied the endogenous growth theory with emphasis on the different models developed by Arrow, Romer and Lucas. We also discussed the assumptions of the endogenous growth theory and highlight the different criticisms in order to bring out the weaknesses of the theory. This unit also examined the relevance of the theory to developing countries.

6.0 TUTOR-MARKED ASSIGNMENTS

i. Explain the features of the endogenous growth theory.
ii. What are the strengths of the endogenous growth model over the exogenous growth model?
iii. Lucas developed the endogenous growth model based on investment in human capital, discuss.
iv. Discuss the relevance of the endogenous growth theory to the Nigerian economy.

7.0 REFERENCES/FURTHER READINGS

Ahuja, H. L. (2016). *Development economics*. New Delhi: S. D. Chand.

Jhingan, M. L. (2011). *The economics of development and planning, 40th edition*. India Vrinda Publications

Howitt, P. (n.d). *Endogenous growth.* Retrieved from www.brown.edu>end...pdf

Onyimadu, C. O. (2015). An overview of endogenous growth models: Theory and critique. *International Journal of Physical and Social Sciences, 5*(3), 498-514

Todaro, M. P. & Smith, S. C. (2015). *Economic development,12th Edition*. USA: Pearson Publishers.

MODULE THREE FACTORS OF GROWTH AND ECONOMIC DEVELOPMENT STRATEGIES

Unit 1 Balanced and Unbalanced Growth Strategy
Unit 2 Import Substitution and Export-Led Promotion Strategy
Unit 3 Capital Formation in Developing Countries
Unit 4 Foreign Trade and Economic Development

UNIT 1 BALANCED AND UNBALANCED GROWTH STRATEGY

1.0 Introduction
2.0 Objectives
3.0 Main Content
  3.1 Balanced Growth Strategy
  3.2 Limitations of Balanced Growth Strategy
  3.3 Unbalanced Growth Strategy
  3.4 Limitations of Unbalanced Growth Strategy

4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References/Further Readings

1.0 INTRODUCTION

Economic development is a serious problem for developing countries with great efforts being put in place by different governments to deal with the situation. Several strategies have been fashioned and employed in a bid to accelerate the tempo of industrialisation in underdeveloped economies with a view to resolving the issue of underdevelopment. Two major schools of thought have come up with strategies to be adopted for economic development to take place. Economists such as Ragnar Nurkse and Rosenstain-Rodan are of the view that the strategy of investment should be so designed as to ensure a balanced and simultaneous investment in a number of industries. While Economists such as Singer and Hirschman believe that there should be concentration of investment in certain strategic industries, that is, unbalanced growth is needed for economic development to take place in an economy. In this unit, we analysize the two doctrines of development, their criticisms and a comparison of the two theories.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

i. Discuss the balanced growth strategy
ii. Explain unbalanced growth strategy.
iii. Give a critical appraisal of both balanced and unbalanced growth strategies

3.0 MAIN CONTENT

3.1.1 Balanced Growth Strategies

The advocates of the balanced growth doctrine are economists such as Rosenstein Rodan, Ragnar Nurkse and Arthur Lewis, with different interpretations to the theory. To some, it means investing in a lagged sector or industry, to others it means simultaneous investment in all sectors, especially manufacturing industries and agriculture (Kindleberger as cited in Jhingan, 2011). The balanced growth theory entails a balance between social and economic overheads (power and energy, drainage system, etc,) and directly productive investment so that all sectors grow in unison (Ahuja 1980 as cited in Metu et al 2018). They believe that there should be simultaneous investment in a number of industries, that is a balanced growth of different industries or investment in lagged sectors of the economy until all sectors are equally developed. Balanced growth strategy recognises the need for expansion and inter-sectoral balance between agriculture and manufacturing so that each of these sectors provides a market for the product of the other and in turn, supplies the necessary raw materials for the development and growth of the other. For instance, in the simultaneous development of agriculture and industrial sector, employment in the industrial sector will lead to increase in the demand for food stuff and raw materials provided by the agricultural sector.

According to Ragnar Nurkse, the vicious cycle of poverty trap can be broken by a simultaneous investment in a large number of industries (Ahuja, 2016). From the supply side of vicious cycle of poverty, he advocates for simultaneous investment in sectors that will help in increasing the supply of goods such as power, agriculture, transport,

irrigation, intermediate goods, etc. The demand side relates to the provision of employment opportunities and incomes so as to induce investment through improved savings resulting from increase in employment and income.

According to Lewis as cited in Todaro and Smith (2015), development programmes should include a balance between agriculture and industry; balance between production for consumption and exports and a balance between the domestic sector and the foreign sector.

3.1.2 Limitations of Balanced Growth Strategy

i). Some economists have criticised Nurkse's doctrine of balance growth on the grounds that what is needed is not balanced growth but a strategy of judiciously-planned unbalanced growth because underdeveloped countries do not have sufficient resources to achieve balanced growth. According to Singer, the fundamental problem with the balanced growth doctrine is its inability to come up with the true problem of underdeveloped countries, which is shortage of resources. When investments are being made simultaneously in a number of new industries, the demand for factors would become competitive. But the supply of factors is inelastic in underdeveloped countries, thus the main argument of the theory breaks down because demand for capital goods does not create its own supply (Nafziger, 2006).

ii). Also establishing industries simultaneously is likely to lead to increase in money and real cost of production and so make them economically unprofitable to operate in the absence of capital equipment, skills, finance and other essential raw materials.

iii). The doctrine of balanced growth advocate for the establishment of new industries instead of considering the possibility of cost reduction in existing ones. With the establishment of new industries, the demand for the products of existing ones will decrease thereby making them unprofitable.

iv). Also the balanced growth doctrine assumes that the relationships between industries are complementary but the limitation of factor supply ensures that the relationship is most times competitive.

v). Above all the balanced growth doctrine seems to have failed as a theory of development. Advocates of this theory assume that persons lacking in skills and entrepreneurial ability can start a new industry, meanwhile in underdeveloped countries necessary skills and other resources for development are lacking. If a country possesses enough skills and resources, the country should not be underdeveloped in the first instance. Therefore, the doctrines are applicable to a subsequent stage of sustained growth rather than breaking a deadlock.

SELF-ASSESSMENT EXERCISES

i. Illustrate the balanced growth strategy

ii. Critically examine the balanced growth strategy.

3.2 The Unbalanced Growth Strategy

Economists such as Singer and Hirschman argue that for development to take place in an economy, there should be an unbalanced growth strategy by concentrating on investment in certain strategic industries. Hirschman advocated for big push in selected sectors of the economy (Onwuka, 2011). According to the paper, underdeveloped countries may follow the method of unbalanced growth by undertaking initial investment in either social overhead capital (SOC) or investment in direct productive activities (DPA) rather than simultaneous investment. Social overhead capital includes investment on education, public health, communication, public utilities such as light, water, drainage and irrigation schemes (Ahuja, 2016; Jhingan 2011). Simultaneous investment in DPA and SOC is not possible due to limited resources and because of the inability of underdeveloped countries to secure adequate resources. Therefore, there is need to determine the sequence of expansion that will maximize induced decision-making. According to Hirschman, the sequence of investment could be from investing in SOC or from investing in DPA first. If

investment is first undertaken in DPA, the shortage of SOC will raise production costs and with time political pressure will stimulate investment in SOC.

From Fig 9, the cost of investment in SOC are measured along the vertical line while that of DPA are measured along the horizontal line. The curves I, II, III are the isoquants showing the different combination of SOC and DPA that result in the same gross national products at a given time. A higher curve shows a higher gross national product on the 45° while the 45°line shows the balanced growth of DPA and SOC though this cannot be simultaneously expanded because of inherent limited ability of the underdeveloped countries to utilise resource.

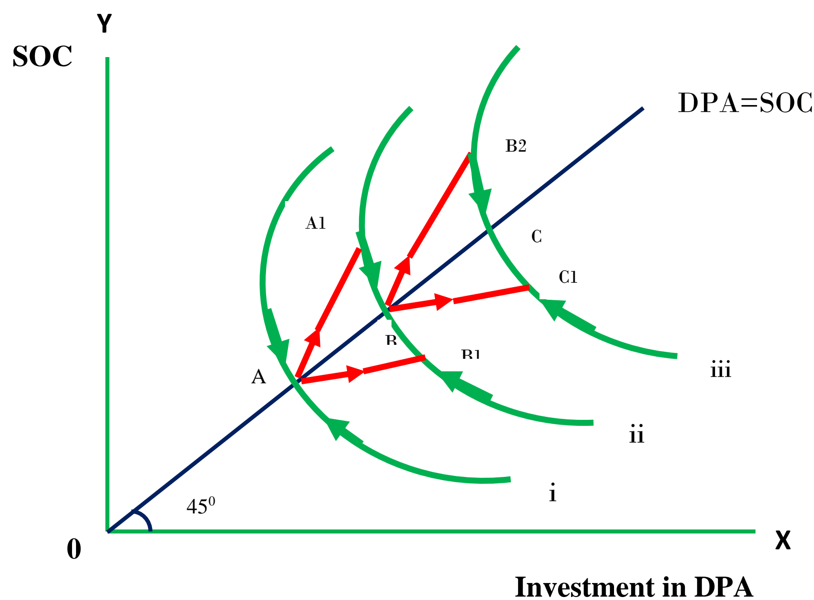

Figure 9: Balanced and unbalanced growth paths.

Source: Ahuja (2016)

Assuming the economy adopts the sequence of development via shortage of SOC. The course followed by the economy would be the line AB_1BC_1C. If we increase DPA from A to B_1 to restore balance, this will be followed by the increase in SOC from B_1 to B. If

there is an increase in DPA to C_1, SOC will have to follow suit until balance is restored at C.

If the path to development is followed via excess capacity of SOC, the economy will follow the line A----A_1-----B---B_2----C. When the economy increases SOC from A to A_1 on the same isoquant, the induced DPA increases from A, to B where the balanced is achieved. With the increased gross national product, the government may undertake further investment in SOC to B_2. This in turn will induce DPA to increase to point C where balance is restored. This is what Hirschman calls self-propelling (Ahuja, 2016).

Having studied the virtues of strategic imbalances, the problem is now how to find the kind of imbalance that is likely to be most effective. According to Mathur (1966) any investment may have both forward linkage (encourage investment in subsequent stages of production) and backward linkages (encourage investment in earlier stages of production). Development should aim at discovering projects with the largest total linkage. In determining the sequence of projects, planning authorities should give attention to pressure creating and pressure relieving investment. Government can provide pressure relieving role to private investors in areas of transport, public utilities, education etc. According to Hirschman, the industry with the highest combined linkage score is iron and steel. The building of it by the government will lead to a spurt of investment and production in a variety of fields both in the stages before and after this industry, in this way economic growth is accelerated. Therefore, for development to take place in underdeveloped countries there should be judiciously planned unbalanced growth.

3.2.1 Limitations of Unbalanced Growth Strategy

i). According to the unbalanced growth strategy, there is need for underdeveloped countries to provide inducement and incentives to private enterprises to undertake investment projects. This assumption is wrong because financial resources are scarce due to lack of savings in the developing countries and this hampers growth. It is not only physical resources that are scarce but also there is limited financial resources to fund the development projects.

ii). Also, the unbalanced growth has been criticised based on the fact that it has the tendency to generate inflationary pressures in the country. When there is investment in SOC or DPA, incomes will rise leading to increase in aggregate demand. If it is not followed up by increase in supply, it will cause increase in prices (Ahuja, 2016).

iii). If private enterprises respond to the inducement and pressure caused by unbalanced growth, it may create imbalances in the economy if it is not followed up by expansion in other linked sectors. This scenario is bound to lead to waste of resources resulting from excess capacity in those industries or sectors responding to inducement.

Despite the criticisms, the doctrine of unbalanced growth is a good attempt at pointing out the way to accelerate economic development for underdeveloped countries (Nafziger, 2006). It shows that unless the SOC path of economic development is followed by the state, it will not encourage private investment in DPA because private enterprise in an underdeveloped country is unable to create the necessary economic surplus required for development.

SELF-ASSESSMENT EXERCISES

i. Illustrate the unbalanced growth strategy

ii. Give a critical appraisal of the unbalanced growth theory.

4.0 CONCLUSION

There has been controversy surrounding balanced and unbalanced growth strategies. Developing countries are encouraged to adopt the unbalanced growth strategy where investment in social overhead capital (SOC) such as manpower, transport, education, etc; is undertaken first then subsequent investments in directly productive activities (DPA). Investment sequence are generated by profit expectations and political pressures. Profit expectations generate sequence from SOC to DPA and political pressures from DPA to SOC. Unbalanced growth has been criticised based on the fact that it has the tendency to generate inflationary pressures waste of resources resulting from excess capacity in the

sectors responding to inducement. We conclude that developing countries should adopt the unbalanced growth strategy due to limited resources.

5.0 SUMMARY

Some economists are of the view that the strategic investment should ensure a balance in investment in a number of industries while some advocate for investment in strategic industries so as to achieve economic development. In this unit, we discussed the two doctrines: balanced and unbalanced growth strategies. Finally, we studied their limitations and implications in developing countries. Doctrine of unbalanced growth is a good attempt at pointing out the way to accelerate economic development in underdeveloped countries.

6.0 TUTOR-MARKED ASSIGNMENTS

i. Explain the balanced growth strategy.
ii. Critic the balanced growth strategy.
iii. With the aid of a diagram, illustrate Hirschman's unbalanced growth strategy.
iv. Give a critical appraisal of the unbalanced growth strategy

7.0 REFERENCES/FURTHER READINGS

Ahuja, H. L. (2016). *Development economics*. New Delhi: S. D. Chand

Jhingan, M. L. (2011). The economics of development and planning. Delhi: Vrinda Publications.

Mathur, A. (1966). Balanced and unbalanced growth- A reconciliatory view. *Oxford Economic Papers, 18*(2), 137-157. Retrieved from https://doi.org/10.1093/orfordjournal-s.oep.a041015

Moczar, J. & Tsukui, J. (1992). Balanced and unbalanced growth paths in a decomposable economy: Contributions to the theory of multiple turnpikes. *Economic Systems Research, 4*(3), 211-221.

Nafziger, E. W. (2006). *Economic development*. New York: Cambridge University Press.

Onwuka, C. E. (2011). *Economic development monograph series 3*.Ekpoma: Pon Publishers

Rauch, J. E. (1997). Balanced and unbalanced growth. *Journal of Development Economics, 54,* 493-518

UNIT 2: IMPORT SUBSTITUTION INDUSTRIALISATION AND EXPORT-LED PROMOTION STRATEGIES

1.0 Introduction
2.0 Objectives
3.0 Main Content
    3.1 Import Substitution Industrialisation Strategy
    3.2 Advantages and Disadvantages of Import Substitution Strategy
    3.3 Export-Led Promotion Strategy
    3.4 Measures for Export Promotion Strategy
4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References/Further Readings

1.0 INTRODUCTION

Trade is an important stimulator of economic growth by increasing world output, enlarging a country's consumption capacities and worldwide markets for products without which developing countries would not be able to grow. Hence, to promote growth and development, trade policies are essential. In this unit, we will study two main traditional trade strategies for development: import substitution industrialisation strategy and export promotion strategy, to see whether developing countries can look inward or outward in order to promote trade for development.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

i. Explain the meaning of import substitution strategy.
ii. Illustrate the advantages of import substitution strategy.
iii. Outline the disadvantages of import substitution strategy.
iv. Discuss the meaning of export promotion strategy.
v. Outline the measures for export promotion strategy

3.0 MAIN CONTENT

Import Substitution Industrialisation Strategy

Import substitution industrialisation strategy (ISI)is a conscious attempt by developing countries to domestically produce commodities that were formerly imported from developed countries (Todaro & Smith, 2015). It involves promoting the emergence and expansion of domestic industries by replacing major imports especially consumer goods such as household appliances, food, textile materials, etc., with locally produced substitutes. That is why it is also referred to as inward-looking development strategy (Onwuka, 2011)

Countries resort to import substitution industrialisation strategy due to balance of payment difficulties and due to negative impact of such imports on the foreign exchange earnings of developing countries. For industries established under ISI to function governments must have to protect them through the use of tariffs and non-tariff barriers to trade. Tax exemptions and subsidies are also used to reduce costs in import competing industries. Import substitution usually begins with the manufacture of durable consumer goods at the final stages of production.

SELF-ASSESSMENT EXERCISE

i. What is import substitution industrialisation strategy?

3.2 The Advantages and Disadvantages of Import Substitution Strategy

3.2.1 The Case for ISI Strategy

(a). Promotion of locally manufactured goods – ISI stresses the need to encourage indigenous "learning by doing" in the manufacturing sector and the subsequent development of appropriate technologies that would be used to tap a country's resource endowments (Jhingan, 2011). This presupposes self-reliance and that is usually accompanied with restrictions on trade, movement of people and policies that restrict the onslaught of multinational enterprises on the national economy.

(b). For achieving self-sufficiency - The case for important substitution rests on the premise that trade has operated historically as a mechanism of international inequality to the disadvantages of developing countries (Onwuka, 2011). They are also justified on the very fact that ISI is adopted for purposes of achieving self-sufficiency in the long run and to save foreign exchange.

(c). Employment opportunities - It is contended that ISI is necessary to provide gainful employment to the underemployed in the industrial sector and to absorb surplus manpower released from agricultural production as a result of increased productivity. This means that as population increases, the growing labour force are engaged in industrial production. ISI also encourages the use of modern labor-saving techniques in productive activity thereby increasing output and efficiency.

3.2.2 The Case against ISI Strategy

(a). The experience of some countries that have adopted the strategy reveals that it is a very bleak strategy which has made their process of industrialisation a costly one. This could be attributed to the fact that some products that would have been imported cheaply are produced at a higher cost.Some countries with such complains are Pakistan, India and some Latin American countries.

(b). Most times foreign firms benefit more from the ISI process than the local firms because they take advantage of the liberal tax and investment incentives which are supposedly offered to local firms to encourage them to produce items whose imports are banned or restricted. Yet, most of the profits made by these foreign firms are remitted abroad, while the left overs usually accrue to the wealthy local industrialists with whom foreign manufacturers cooperate under political and economic cover (Todaro & Smith, 2015).

(c). Rather than being a saver of foreign exchange, the policy has tended to consume available foreign exchange because the established industries need it for their operations (Nafziger, 2006). The fact remains that developing countries lack intermediate goods and capital equipment to start import substitution industries. Consequently, the need for

imports is much greater when this strategy is being implemented than otherwise. That being the case, the indirect expenditure of foreign exchange on inputs and capital goods needed for import substitution industries far exceeds the direct savings of foreign exchange.

SELF-ASSESSMENT EXERCISES

i. Discuss the advantages of import substitution industrialization strategy.
ii. Explain the disadvantages of import substitution industrialization strategy

3.3 Export Promotion or Export-Led Strategy

The promotion of exports of developing countries, either primary or secondary, has long been considered a major ingredient in any viable long-run development strategy. Export promotion strategy is a trade strategy in which there is bias of incentive towards production of import substitutes (Metu et al., 2018). Export promotion is a purposeful governmental effort to expand the volume of a country's exports through export incentives and other means in order to generate more foreign exchange and improve the current account of its balance of payments. The essence of promoting exports in developing countries is to overcome disequilibria in the balance of payment (Onwuka, 2011).

Todaro and Smith (2015) opine that before embarking on export promotion, comprehensive market surveys are carried out to ascertain potential markets. Also, promotion of dynamic commodities that command demand in the world market and price elasticity should be sought and encouraged; while those with doubtful demand abroad and hence low foreign exchange earnings base should be discouraged.

Similarly, while it is encouraged to increase the production of non-traditional items needed by both developed and developing countries, it is equally essential that a careful examination of the composition of these exports in items and their prospects in the world market be carried out. This is necessary to decide which exports should be increased, promoted or be left out of consideration (Onwuka, 2011).

3.4 Measures to Promote Export Promotion Strategy

For export promotion strategy to be effective, certain measures are considered essential and they include:

1. The government should maintain reasonable price stability so that the export commodities will be demanded at the international markets.
2. The realisation of production targets set in the agricultural, mineral and industrial sectors of the economy is of utmost importance.
3. The government can use fiscal policy to restrain and reduce the growth of domestic consumption of export products so as create surpluses for exportation.
4. Provision of credit, insurance, transport and other vital facilities to aid the required exports. In addition, there is the need for tax concession to exporters. This could be in the form of no taxes on imported raw materials and certain other components used in the manufacture of exportable goods.
5. The commodity should be able to meet up with international competition. This can be achieved by using modern export-oriented industries, introduction and enforcement of quality control and compulsory pre-shipment inspection of various exportable commodities for the sake of quality assurance (Jhingan, 2011). This will help to ensure that the goal of export-led industrialisation strategy is achieved in terms of competitiveness.
6. Participation in industrial exhibitions and trade fairs abroad and promotion of visual commercial publicity for the purpose of export promotion. This is in addition to setting up of Export Promotion Council for major export and welcoming foreign participation in trade matters because foreign firms can bring the contacts and production know-how needed for penetrating global markets.
7. Providing automatic access to foreign exchange and eliminating export monopolies both local and foreign. This can be done through facilitating access to intermediate inputs and capital goods needed for the production and expansion of export commodities.

SELF-ASSESSMENT EXERCISES

i. What is export promotion industralisation strategy?
ii. Discuss the ways to promote export-led industrialisation strategy.

4.0. CONCLUSION

Import substitution strategy (ISI) requires a deliberate effort to replace imports by promoting the emergence and expansion of domestic industries. While export promotion involves government efforts to expand the volume of a country's exports through export incentives and other means so as to generate more foreign exchange and improve the balance of payment or achieve other macroeconomic objectives. Ways through which government can improve its trade policy is by erecting tariff barriers or quotas on certain imported commodities and try to set up a local industry that will produce similar goods.

5.0 SUMMARY

We discussed the meaning of import substitution industrialisation and export promotion strategies. The advantages and disadvantages of import substitution industrialisation strategies were also discussed. Finally, we studied the measures that developing countries can adopt in order to improve the rate of exportation.

6.0. TUTOR-MARKED ASSIGNMENTS

i. Why is import substitution industrialisation strategy important as a trade policy?
ii. Differentiate import substitution industrialization strategy from export promotion strategy.
iii. Identify the measures that can be used by policy makers to improve the rate of exportation of goods in Nigeria.

7.0 REFERENCES/FURTHER READINGS

Ahuja, H. L. (2016). *Development economics*. New Delhi: S. D. Chand.

Amin, S. (1976). *Unequal development: An essay on the social formations of peripheral capitalism*. New York: Monthly Review Press.

Nafziger, E. W. (2006). *Economic development*. New York: Cambridge University Press.

Onwuka, C. E. (2011). *Economic development monograph series 3*.Ekpoma: Pon Publishers

Todaro, M. P. & Smith, S. C. (2015). *Economic development*,*12th Edition*. USA: Pearson Publishers

UNIT 3: CAPITAL FORMATION AND ECONOMIC DEVELOPMENT

1.0 Introduction
2.0 Objectives
3.0 Main Content
  3.1 Meaning of Capital Formation
  3.2 The Role of Capital Formation in Developing Countries
  3.3 Reasons for Low Rate of Capital Formation in Developing Countries
  3.4 Sources of Capital Formation in Developing Countries
4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References/Further Readings

1.0 INTRODUCTION

The rate of economic growth depends mostly on the rate of investment and capital output ratio. Achieving these two objectives depends on the technology used for productive activities. This means that if we want to achieve economic growth, investment or capital formation must be raised while lowering capital output ratio. In this unit, we will discuss the meaning of capital formation, the determinants of capital formation, the role as well as sources of capital formation in developing countries.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

i. Explain the meaning of capital formation
ii. Outline the role of capital formation in developing countries
iii. Describe the reasons for low rate of capital formation in developing countries
iv. Illustrate the sources of capital formation in a developing economy

3.0 MAIN CONTENT

3.1 The Meaning of Capital Formation

Capital is one of the basic factors of production. It is accumulated assets that can be used to generate income. Capital can be physical assets such as plants, machinery, equipment, building, etc., or human capital such as knowledge, skills and abilities of employees, used for production. Capital formation is the increase in the stock of real capital in an economy (Ahuja, 2016). It means producing more capital goods used for further productive

activities. Another name for capital formation is capital accumulation or investment. Over time, when an economy invests, they add to the stock of tools, machinery, buildings etc. According to Ragnar Nurkse as cited in Ahuja (1980) capital formation means that an economy does not use up its current productive activity for immediate consumption rather direct some to the production of capital goods such as machine, plant and equipment, tools and instruments and transport facilities. The essence is to divert some part of the society's current available resources for the purpose of increasing the stock of capital that will be needed in future for the expansion of consumable output. This means that in order to accumulate capital goods, some part of current consumption has to be sacrificed (Jhingan, 2011). The greater people are willing to abstain from present consumption, the greater the extent the society will devout resources to new capital formation. If the society consumes all that is currently produced, future productive capacity will fail as a result of wear and tear by present capital equipment.

Capital accumulation can be made possible through *widening of capital*, that is duplicating existing technique, or through *deepening of capital*, that is use of capital-intensive technique. This is to show that capital accumulation facilitates technological progress and improvement. According to Ahuja (2016), in a modern enterprise economy, the process of capital formation consists of three stages: (a) the increase in the volume of savings, (b) mobilization of savings through financial and credit institution and (c) the act of investment so that resources are used for production of capital goods.

SELF-ASSESSMENT EXERCISE

i. What is capital formation?
ii. Differentiate between deepening of capital and widening of capital.

3.2 The Role of Capital Formation in Developing Countries

(i). Increase in Productivity – It adds to the productivity of both the individual and the economy as a whole. Capital equipment on a large scale increases productivity in agriculture, mining, exploitation of natural resources, constructions in the industrial

sector as well as increasing the social overhead capital. It is capital formation that leads to fuller utilization of available resources.

(ii). Increase in National Income- Increase in productivity leads to increase in the size of national output and income thereby solving the problems of inflation and balance of payment, and saving the economy from the burden of debt.

(iii) Technological progress of the economy – Capital formation leads to technical progress which helps realize the economies of large scale production and increases production. It also helps to provide machines, tools and equipment for the labour force.

(iv). It creates employment opportunity– Investment in capital equipment increases production and creates employment opportunities for the increasing labour force. When an economy uses capital intensive mode of production, different individuals are employed to manage and handle those machines.

(v). Improvement in welfare and economic development – Capital formation makes development possible even with rising population (Onwuka, 2011). When population is rising, increase in per capita output is related to the increase in capital-labour ratio. But countries aiming at raising capital output ratio faces a problem. When population is increasing rapidly, it becomes difficult to have enough savings for investment due to low per capita income that reduces the propensity to save and invest. Hence, the only solution is rapid capital formation in such a country.

Also, through capital formation, different industries are established, levels of income are increased and wants are satisfied. With improved income, people consume variety of goods and services leading to improvement in standard of living and increase in economic welfare.

(vi). Reduction in the debt burden - Capital formation dispenses the need for foreign aid and loans by making countries self-sufficient. When a country borrows, it imposes a heavy debt burden on the future generations with debt repayments and levying of higher taxes. Capital formation increases national income, makes a country self-sufficient and gradually reduces the rate of borrowing.

SELF-ASSESSMENT EXERCISE

i. Explain the importance of capital formation in developing countries.

3.3 Reasons for Low Rate of Capital Formation in Developing Countries

The major reasons for low rate of capital formation in developing countries are as follows:

(i). Low Level of Domestic Savings- The level of savings in developing countries is very small due to the low level of national income or per capital income. The low relative real income also reduces their capacity to save. People in developing countries consume much of their income leaving very little for investment purposes. People in developing countries with large incomes, spend them on conspicuous consumption such as investing in, accumulation of expensive gold and jewelry, rather than using it for productive investment. Hence, they are caught up in the vicious circle of poverty, that is, low income—small savings—low investment—less capital—less productivity, ending in low income and the cycle continues.

(ii) Lack of Enterprise - Lack of entrepreneurial ability is another factor responsible for the low rate of investment in developing countries. According to Schumpeter, good and daring entrepreneurs are the focal point in the process of economic development (Ahuja 2016). The problem in developing countries is that their entrepreneurs are interested in making quick returns. They are not daring enough to bear large risks involved in making capital goods. If investment is to be increased in developing countries, the government must take up entrepreneurial role and also be ready to promote and encourage those engaged in entrepreneurial activities.

(iii). Weak Inducement to Invest - According to Nurkse, the small size of the market is another reason why investment and capital formation are low in developing countries because it hinders initiative and enterprise. The small size of the market also limits the use of capital equipment in the production of goods and services for the domestic market.

According to the vicious circle on the demand side of capital formation, the inducement to invest may be low due to small buying power of the people, caused by low real income, which, again is caused by low productivity from the small amount of capital used in production and the cycle continues by keeping the rate of capital formation low.

(iv). Poor Financial Institutions – Poor financial and credit institutions to mobilise and procure fund is another reason for low capital formation in developing countries. Large capital expenditures are needed for productive purposes, but this seems difficult because of lack of properly developed financial institutions such as capital and stock markets, banks and loan institutions. Hence, capital formation is jeopardized because entrepreneurs cannot access fund for investment.

(v). Lack of Capital Equipment – In underdeveloped economies, the rate of capital formation remains low due to lack of capital equipment. In such countries, total capital investment are hardly 5% to 6% of national income, whereas they are 15% -20% in developed countries (Onwuka, 2011). The rate of capital formation remains at a low level in developing countries because it is not possible to replace the existing capital equipment due to depreciation in such countries.

(vi). Lack of Economic Overhead – The existence of economic overheads is essential to make fruitful investment and to encourage enterprise. But economic overheads like power, water, communication, transportation, etc, are lacking in developing countries, it retards enterprise, investment activities and the path to capital formation.

(vii). Demographic Reasons - Developing countries possess such demographic features which keep the rate of capital formation at a low level (Todaro & Smith, 2015). The growth rate of population is very high. As a result, the per capita income is low. Moreover, the income is spent on consumer goods in an effort to take care of the family which with little or nothing saved for capital formation. Beside the rapid increase in population aggravates the shortage of capital because large investments are required to equip the growing labour force. Thus demographic bottlenecks inhibit the rate of capital formation in developing countries.

SELF-ASSESSMENT EXERCISE

i. Discuss the reasons for the low rate of capital formation in developing countries.

3.4 Sources of Capital Formation in Developing Countries

The sources of capital formation in developing countries are discussed are as follows:

i) Savings: Savings is a matter of habit, which can be inculcated in people using information and social education. Savings drivesthrough issuing of saving certificates such as government bonds and annuities carrying a high rate of interest may also serve as means of mobilizing savings. Saving drive require resolute efforts to persuade people to save in their own interest or in the interest of the family, for education purposes, for acquiring asset such as buildings or as a safeguard against old age, sickness or emergency. Lottery and tax exemptions on the purchase of government bonds can also serve as further incentives to savings for capital formation (Jhingan, 2011).

ii) Increase in National Income: Another important step is to increase the national output or income which would raise per capita income. This can be done by utilising the existing techniques and employing resources more efficiently, by utilising unused resources productively and by increased division of labour.

iii) Improvement and Establishment of Financial Institutions: It is common knowledge that much of the unspent current income is hoarded in cash, jewels, gold and so on by the people. Therefore, there is the need to establish financial institutions, encouraging people to start off life insurance, establishment of savings banks and promoting savings by cooperative societies where small savers can safely deposit their money with confidence. The central bank can also help in developing the capital and money markets as a way of boosting peoples' confidence in long term saving.

iv) Monetary and Fiscal Policy Measures: Mobilization of voluntary savings for capital formation are very difficult in developing economies. The government can adopt various fiscal policy and monetary policy measures that can help to mobilise

savings. These measures could be achieved by using surplus budgeting through taxes, increase or reduction in government expenditures, expansion of the export sector, raising money by public loans and even through deficit financing. Similarly, the government can increase savings and earn large profit by being more prudent and efficient in running public enterprises. Above all, the government should evolve a growth-oriented long-term savings policy so that savings should increase automatically as development gains momentum (Ahuja, 2016).

v) **Public Borrowing:** Public borrowing is a useful tool for diverting resources from unproductive to productive channels. Though, due to low levels of income and savings and high propensity to consume, the use of public borrowing is limited in developing countries. Also, there is lack of organized money and capital market to facilitate public borrowing in developing countries. The government can mobilise domestic savings for productive investment by establishing public corporations. Further, intermediate agencies such as savings banks, commercial banks, insurance companies, community banks and social security institutions to facilitate public borrowing. To make public borrowing a success, concerted campaign through propaganda and social education is essential.

vi) **Foreign Capital:** Foreign capital can be obtained through external finance in form of foreign loans, grants/aid and foreign investments. All these sources expand the frontiers of capital available to the recipient country. For example, grants which are not normally rapid and foreign loans can be critical for capital accumulation because they help intransferring financial resources to the recipient countries. The problem with loans is that if not channeled towards productive ventures, it will not serve the cause of capital formation. Foreign investments also help in the transfer of technology, know-how and infrastructures, which ordinarily would be difficult to obtain without such investments.

vii) **Favourable External Trade:** The gains from foreign trade played critical role in the development of the present advanced countries. In fact, the profits earned by their trading companies at the infancy of their development and the export of

finished goods to their colonies constituted the backbone in the process of capital accumulation of the major industrialized countries of Europe during the 19th-20th centuries (Onwuka, 2011). Efforts, therefore, need to be intensified to urge the developed trading partners of developing countries to ameliorate the many obstacles on the path of increased exports of developing counties. This is with a view to letting external trade assume its historic responsibility of capital accumulator for development on behalf of developing countries.

SELF-ASSESSMENT EXERCISES

i. Discuss the sources of capital formation in developing countries

ii. How can foreign investment serve as a source of capital formation in Nigeria?

4.0 CONCLUSION

Capital formation raises the level of national output which in turn raises the rate and level of national income. Capital formation is regarded as one of the principal solutions to the complex problems of economic development in developing countries. There are different sources through which developing countries can accelerate capital formation so as to achieve economic growth.

5.0 SUMMARY

Capital formation or accumulation is also known as investment and is regarded as one of the important and principal factors in economic growth and development. The vicious cycle of poverty in developing countries can be broken through capital accumulation. It is noticed that the low level of income in developing countries leads to deficient demand, production and investment. Capital formation can help to solve these problems by increasing supply of tools and equipment, improving technological progress, increasing productivity and creating employment opportunities.

6.0 TUTOR-MARKED ASSIGNMENTS

i. What are the reasons for the low rate of capital formation in Nigeria?

ii. Discuss the major determinants of economic growth in developingcountries.

iii. Explain the external sources of capital formation in developing countries.

7.0 REFERENCES/FURTHER READINGS

Aboyade, O. (1983). *Integrated economics: A study of developingcountries*. London: Wesley Publishing.

Ahuja, H. L. (1980). *Modern economics*. New Delhi: S. D. Chand

Ahuja, H. L. (2016). *Development economics*. New Delhi: S. D. Chand.

Jhingan, M. L. (2011). The economics of development and planning. Delhi: Vrinda Publications.

Onwuka, C. E. (2011). *Economic development monograph series 3*.Ekpoma: Pon Publishers

Todaro, M. P. & Smith, S. C. (2015). *Economic development, 12th Edition*. USA: Pearson Publishers.

UNIT 4: FOREIGN TRADE AND ECONOMIC DEVELOPMENT

1.0 Introduction
2.0 Objectives
3.0 Main Content
 3.1 Meaning of Foreign Trade
 3.2 The Role of Foreign Trade in Economic Development
 3.3 The Limitations of Foreign Trade in Economic Development
4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References/Further Readings

1.0 INTRODUCTION

The role of foreign trade in economic development is considerable with both the classical and neoclassical attaching so much importance to it. They regard it as an engine of growth in any economy. Although, there are some scholars who hold opposing view that international trade leads to inequality with rich countries becoming richer at the expense of the poor countries. In this unit, we shall discuss the meaning of foreign trade, we shall also study how international trade promotes economic development. Finally, we will discuss the limitations of foreign trade in achieving economic development in LDCs.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

i. Define and explain the meaning of foreign trade.
ii. Outline the role of foreign trade in economic development.
iii. Describe the limitations of foreign trade in developing countries.

3.0 MAIN CONTENT

3.1 Foreign Trade: Meaning and Definition

Trade is the exchange of goods and services. It is divided into internal (domestic) trade and international (foreign) trade (Todaro & Smith, 2015). Foreign trade refers to the

transfer of goods and services from one country to another, that is, it extends beyond the political boundaries of the countries engaged in it (Dubey, Mishira, Iyer & Mishira, 2015). Economics concepts (2012) defines it as trade across international boundaries and it is costlier than domestic trade (trade within boundaries). Countries engage in foreign trade because production of goods and services varies in different countries of the world.

International trade enables countries to sell their domestically produced goods to other countries (Abdullahi, Sokoto & Safiyanu, 2013). Countries that engage in foreign trade usually operate under one umbrella or the other, such as multilateral, bilateral, as well as regional agreement. However, the General Agreement on Trade and Tariffs (GATT) which was replaced by the World Trade Organisation (WTO) in 1993 is the organization that controls all registered international trade members' nations (Cooper, 2012). Countries may concentrate in producing goods they are good at while importing other goods they may need from other countries. This type of specialization is referred to as advantage (Jhingan, 2011).

A country has absolute advantage when it can produce and sell at a lower cost than any other country or when it is the only country that can provide such a product. Similarly, a country enjoys comparative advantage when they specialise in the product that it can produce most readily and cheaply and import those goods that foreign countries can produce readily and cheaply.

3.1.2 Barriers to Foreign Trade

Trade barriers are restrictions on international trade imposed by the government and designed to impose additional costs or limits on imports and/or exports in order to protect local industries (Abdullahi et al., 2013). The additional cost results in a higher price of importation and make local production competitive. Some trade barriers are discussed below:

i) Tariffs- Tariffs also called duties are taxes imposed by the government on imported goods and services. They can be implemented to raise the cost of products and make them more expensive than locally produced goods and

services. A tariff may be a charge per unit of product or it may be a percentage of the value of the goods in question. Any tariff makes import costly and less able to compete with domestic product.

ii) Non-tariffs – These are barriers that are imposed by government through measures other than tariffs. Non-tariff measures include import quotas, subsidies, exchange control, embargos or limit on quantity of goods to be imported. Government may grant subsidies to local producers in order to make their products competitive; or may establish quantity and content requirements for imported goods.

Exchange control refers to laws requiring a foreign exchange earner from export to sell the foreign exchange to a country agency. By controlling the amount of foreign exchange sold to companies, the government controls the amount of products that can be imported. Limiting imports and encouraging exports helps a country to create a favourable balance of trade.

iii) Natural barriers – Natural barriers to foreign trade includes distance and language. People who cannot communicate effectively may not be able to negotiate trade agreements.

SELF-ASSESSMENT EXERCISES

i. Discuss the meaning of foreign trade.
ii. What are the barriers to foreign trade?

3.2 Importance of Foreign Trade

- Foreign trade possesses great importance for developing countries by providing the urge to develop the knowledge and experience that accelerates development. When a country specialises in the production of a few goods due to international trade and division of labour, the commodities which are produced cheaper are exported in exchange for what others can produce at a lower cost. This leads to higher level of output and gains from trade (Abdullahi et al., 2016). The gains from trade helps to break the vicious cycle of poverty because with trade, there is increase in national income which in turn raises output and the growth rate.

- Developing countries are hampered by the small size of the domestic market. The small size of the market is as a result of low per capital income and purchasing power of people. With international trade, there is wider market which increases the inducement to save and invest through more efficient resources. The introduction of international trade opens the possibility of a 'vent for surplus' in LDCs (Jhingan 2011). In developing countries, land and labour are underutilized especially in the subsistence sector. Foreign trade provides the domestic economy more opportunities to produce their primary products for exportation to foreign countries. The vent for surplus theory, as applied to an LDC is explained using Figure 10.

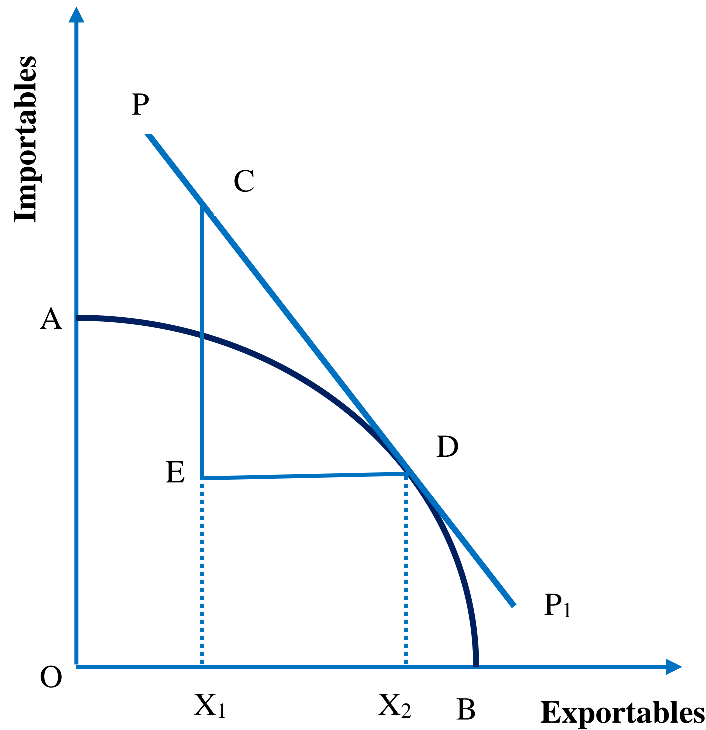

Figure 10: Graphical representation of surplus with international trade

Source: Jhingan, (2011)

Figure 10 shows that before trade with underutilized resources, the country is producing and consuming $OX_1$of primary products and X_1E of manufactured products at point E inside the production possibility curve AB. With the opening

up to foreign trade, the production point shifts from E to D on the same production possibility curve AB. Now utilisation of the utilised land and labour enables the country to increase its production of primary exportable products from OX_1 to OX_2without sacrificing the production of other goods and services. Given the international terms of trade line PP_1 the country exchanges ED (=X_1, X_2) more of primary exportable against EC larger manufactured imports. Many underdeveloped countries specialize in production of one or more staple commodities and if efforts are made to export them, they tend to widen the market. And with the given production function, the resources are efficiently employed and allocated. Hence, unemployment is reduced, domestic savings and investment are increased; also there is greater forward and backward linkages with other sectors of the economy.

- Foreign trade helps in the exchange of domestic goods with low growth potential for foreign goods with high growth potentials. For instance, staple commodities and raw materials are exchanged for machinery, capital goods and semi- finished goods needed for development. Developing countries being deficient in capital goods and materials can accelerate the pace of development by importing capital goods from developed countries and establish social and economic overheads capital as well as directly productive activities.
- International trade possesses educative effect in developing countries. Under developed countries lack critical skills and technical know-how needed for development but through foreign trade, they can overcome these weaknesses. According to Haberler as acted in Jhingan (2011) foreign trade is the means and vehicle for dissemination of technical knowledge, the transmission of idea, managerial talents and entrepreneurships. These imported skills and technological know-how are stimulus for technological progress in developing countries. Foreign trade facilitates selective borrowing of ideas and skills from developed countries and adopting them in accordance with their factor endowments.

- International trade provides the basis for the importation of foreign capitals into the developing countries volume of trade. Foreign capital helps in increasing employment opportunities by increasing output and also smoothen the balance of payments and inflation pressures.
- International trade indirectly benefits developing countries by fostering healthy competition and checking inefficient monopolies. Healthy competition is very vital for the development of export as well as for checking inefficient exploitative monopolies that may be established in the domestic economy.

3.3 Limitations of Foreign Trade

- Economists such as Prebish, Singer and Myrdal has criticised foreign trade on the ground that it impedes development. Their major arguments as identified by Jhingan (2011) are:
- Strong backwash effect on developing countries - According to Myrdal (1956) trade operates with a fundamental bias in favour of richer countries and to the detriment of developing countries. This is because the rich countries have large base of manufacturing industries. By exporting their industrial products at cheap rates to developing countries, they tend to price out the domestic small scale industries and convert the backward countries into producers of primary products. Primary products are prone to price fluctuations because the demand for primary products is inelastic in the export markets. When the price of their products rises at the world market, they will not benefit from it. Most times, increased export earnings leads to inflationary pressures, misallocation of investment, expenditures and development difficulties.
- According to Prebisch, there has been secular deterioration in the terms of trade of developing countries. This means that there has been an international transfer of income from the poor to the rich countries and that the gain from international trade have gone more to developed countries at the expense of the developing countries thereby reducing their real income and capacity for development.

- Many developing countries have many of their major proportion of aggregate output being determined by international transactions (Abdullahi, Safiyanu & Soja 2016).

SELF-ASSESSMENT EXERCISES

i. What are the contributions of foreign trade to economic development in developing countries

ii. Discuss the limitations of foreign trade in a developing country.

4.0 CONCLUSION

Foreign trade also known as international trade acts as engine of growth in developing countries. This is against the notion by the opposition that foreign trade is a mechanism of international inequality. Foreign trade has contributed in enlarging the size of the market and scope of specialisation; it leads to the importation of foreign capital and new ideas, technical know-how and managerial talents. It also fosters healthy competition in the domestic economy. We cannot say that the development of the export sector has been at the expense of the domestic sector. This means that foreign trade does not stand in the way of domestic investment rather it helps to accelerate growth in developing countries.

5.0 SUMMARY

In this unit, we studied foreign trade, barriers and its role in economic development in developing countries. Foreign trade allows for more efficient allocation of resources through economies of scale as well as through an increased competition. Finally, we discussed the limitations or disadvantages of foreign trade in developing countries.

6.0 TUTOR-MARKED ASSIGNMENTS

i. Foreign trade can also be referred to as international trade. Briefly explain.

ii. Enumerate the role of foreign trade in accelerating economic development.

iii. Outline the different limitations of foreign trade to developing countries.

7.0 REFERENCES/FURTHER READINGS

Abdullahi, A. O., Safiyanu, S. S. & Soja, T. (2016). International trade and economic growth: An empirical analysis of West Africa. *IOSR Journal of Economics and Finance, 7*(2), 12-15. Retrieved from http://www.iosrjournals.org

Abdullahi, Y. Z., Sokoto, A. A. & Safiyanu, S. S. (2013). An analysis of the relationship between foreign trade and economic growth in Africa. *Economic and Financial Review, 3*(3), 1-10. Retrieved from http://www.businessjournals.org/efr

Ahuja, H. L. (2016). *Modern economics*. New Delhi: S. D. Chand.

Economic Concepts (2012). Home trade and international trade, definition and difference. Retrieved from http://www.economicsconcepts.com/home-trade-and-international-trade.html>

Hartman, S. W. (2010). Trade barriers. *Academy of Taiwan Business Management Review, 6*(1), 32-43.

Jhingan, M. L. (2011). *The economics of development and planning*. Delhi: Vrinda Publications.

Dubey, D. k., Mishira, M., Iyer, M., & Mishira, S. K. (2015). Business Economics. India: Himalaya Publishing House.

Onwuka, C. E. (2011). *Economic development monograph series 3*.Ekpoma: Pon Publishers

Todaro, M. P. & Smith, S. C. (2015). *Economic development,12th Edition*. USA: Pearson Publishers.

http://www.ariafilaloblog.com/wp-content/uploads/2017/10/international-trade.jpg