

IB Diploma: Economics

**Section 4: Development  
Economics  
COURSE  
COMPANION**

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**tutor2u** 

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## Economic development

### Nature of economic growth and economic development

#### What is economic development?

- Development means many things to many people. It is fundamentally about people development over time. As of 2015, 800 million people still live below \$1.90 per day (PPP)
- Nobel Economist **Amartya Sen** writing in “Development as Freedom”, sees development as concerned with improving the freedoms and capabilities of the disadvantaged, thereby enhancing the overall quality of life
- **Amartya Sen** pursues the idea that human development provides an opportunity to people to free themselves from deep suffering caused by
  - Early / premature mortality
  - Persecution and intolerance
  - Starvation / malnutrition
  - Illiteracy



**Amartya Sen**

Improving and deepening people's freedoms and capabilities lies at the heart of economic development



**Joseph Stiglitz**

Development is about transforming the lives of people, not just transforming economies



**Angus Deaton**

The absence of state capacity – that is, of the services and protections that people in rich countries take for granted – is one of the major causes of poverty and deprivation around the world

According to **Professor Ian Goldin** of Oxford University

- “Development years ago was dominated by rates of economic growth and progress in lifting per capita incomes. This is now a much smaller aspect of development”
- “Every year new concepts and dimensions are introduced and development economics is now branching out into disciplines such as behavioural economics”
- “What is development about? It is about the ability to shape our own lives. It requires information, literacy, participation and capabilities”

**Michael Todaro** specified three objectives of development:

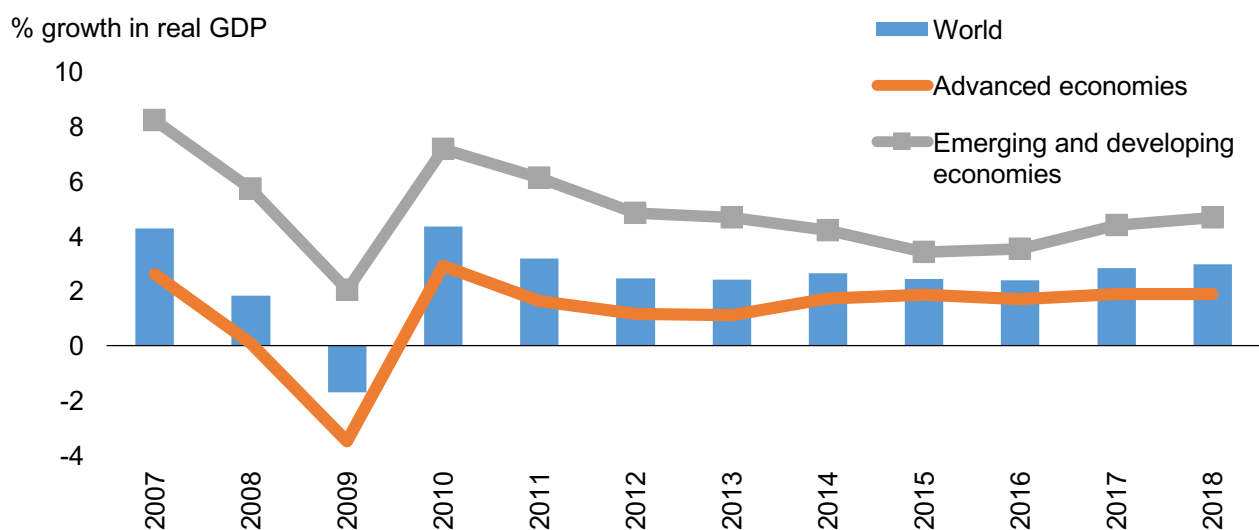
1. **Life sustaining goods and services:** To increase the availability and widen the distribution of basic life-sustaining goods such as food, shelter, health and protection services.
2. **Higher incomes:** To raise levels of living, including, in addition to higher incomes, the provision of more jobs, better education, and greater attention to cultural and human values, all of which will serve not only to enhance material well-being but also to generate greater individual and national self-esteem
3. **Freedom to make economic and social choices:** To expand the range of economic and social choices available to individuals and nations by freeing them from servitude and

dependence not only in relation to other people and nation-states but also to the forces of ignorance and human misery.

## The Difference between Growth and Development

- **Economic Growth**
  - A sustained rise in a country's productive capacity
  - An increase in real value of GDP / GNI per capita
  - Increases in the productivity of factors of production
- **Economic Development**
  - Progress in expanding economic freedoms
  - Sustained improvement in economic and social opportunities
  - Growth in personal and national capabilities

## Developed and Developing Country Growth



“Emerging economy” is used to describe an economy in the process of rapid growth and industrialisation.

## Common Features of Emerging Economies

- Economies making a transition from heavy dependency on the primary sector
- Rapid industrialisation (i.e. development of secondary & tertiary sectors)
- Have potential to become developed economies
- Faster long-term economic growth than most developed economies
- Many inhabitants still in poverty, though economic growth is taking many out of poverty
- Businesses struggle to access global markets (e.g. trade barriers)

## How Economic Growth can spur Development

Sustained growth can spur development in several ways:

1. Lifts per capita incomes and raises people out of extreme poverty
2. Increased per capita GDP/GNI gives households and businesses greater financial resources to save (see the Harrod Domar growth model)
3. Creates new jobs providing a flow of incomes for people in work
4. Higher incomes can also reduce income and wealth inequality
5. Faster economic growth generates higher profits which can then be reinvested – promoting increased productivity and capacity

6. Growth can accelerate changes in patterns of production e.g. a shift away from a dual economy towards investment in light and heavy manufacturing and services such as business services, financial services and tourism
7. Economic growth can generate higher tax revenues for the government – providing more funds to finance public and merit goods and welfare spending

However – important to realise that there are disadvantages from economic growth i.e. economic and social costs from externalities and the social costs of rising inequality. Growth is probably a necessary but insufficient condition for sustained human development – it can underpin gains in health, education and per capita incomes but many factors determine the development process.

### Risks from rapid economic growth

- Risks of higher inflation and higher interest rates
  - Fast-growing demand can lead to demand-pull and cost-push inflation – this leads to a conflict between macro objectives
  - The central bank may decide to raise interest rates to control inflation
- Environmental effects
  - More negative externalities such as pollution & waste
  - Risk of unsustainable extraction of finite resources – i.e. fast growing countries may cause a long-run depletion of natural resources
- Inequalities of income and wealth
  - Rapid increases in real national income can lead to a higher level of inequality and social divisions
  - Many of the gains from growth may go to only a few people

### Economic Growth for Regions of the World

(f) Data in 2016 is a forecast in the January 2016 World Bank Global Economic Prospects

Country Groups	2013	2014	2015	2016f
BRICS	5.7	5.1	3.9	4.6
Developing economies	5.3	4.9	4.3	4.8
High-income economies	1.2	1.7	1.6	2.1
Low-income economies	6.4	6.1	5.1	6.2
<b>World economy</b>	<b>2.4</b>	<b>2.6</b>	<b>2.4</b>	<b>2.9</b>
<b>Regions / Developing Countries</b>				
Developing East Asia and Pacific	7.1	6.8	6.4	6.3
Developing Europe and Central Asia	3.9	2.3	2.1	3.0
Developing Latin America and the Caribbean	3.0	1.5	-0.7	0.1
Developing Middle East and N. Africa	0.6	2.5	2.5	5.1
Developing South Asia	6.2	6.8	7.0	7.3
Developing Sub-Saharan Africa	4.9	4.6	3.4	4.2

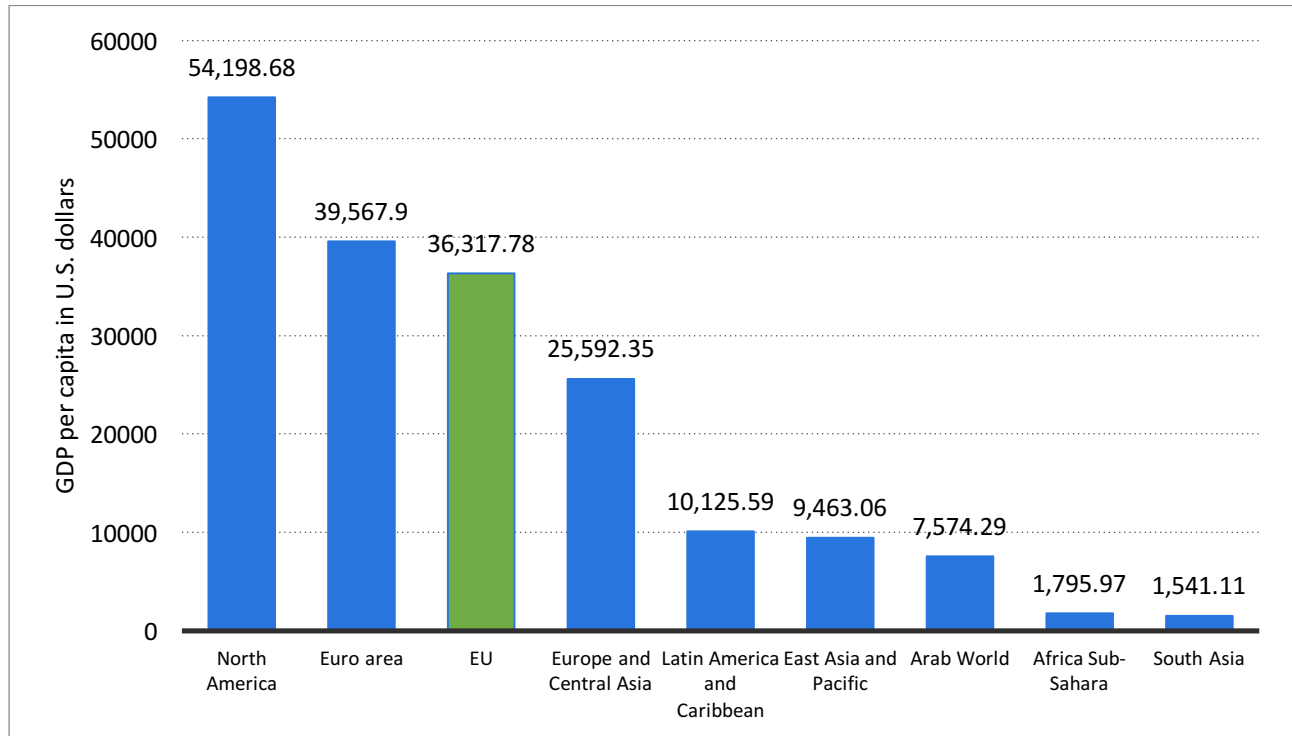
### Reasons for Positive Medium-Long-Term GDP Growth Trends for Emerging Markets

1. Urbanization process continues
2. Industrialization – especially in East Asia and SS Africa
3. Population growth (demographic dividend)
4. Per capita income growth
5. Rise of middle classes and consumer society
6. Focus on supply-side reforms to drive more competition and productivity

7. Improved human capital to absorb and then commercially exploit existing and new technologies developed in developed countries
8. Technological innovation in many emerging markets (especially in Korea, China, India)

### Per Capita Incomes in the World by Region in 2014

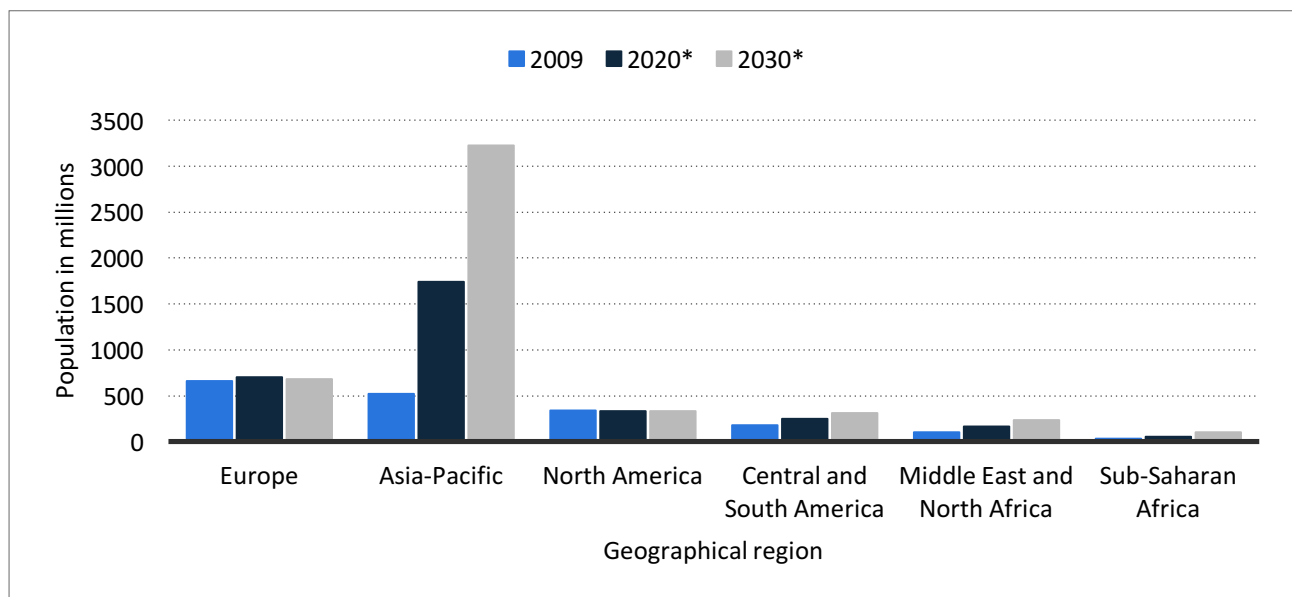
GDP per capita (\$) in selected global regions measured at current prices in 2014



### Projected changes in the global middle class

Forecast of the global middle class population from 2009 to 2030, by region (in millions)

Source: Brookings Institution 2016



### Common Characteristics of Economically Less Developed Countries

No country is the same, but these are some of the frequently-found characteristics:

1. Relatively low incomes per capita and a low level of absolute savings
2. Lower absolute levels of productivity (labour and capital)
3. High dependency on export incomes from commodities / low export diversification
4. Large share of the population living in rural areas and employed in agriculture
5. Limited scope and support provided by a welfare system
6. A larger informal sector for example in partial subsistence farming
7. Many industries in low-income countries are distanced from technological frontiers
8. Relatively fast growth of population and a younger average age
9. Rapid urbanization and large-scale rural-urban migration
10. Weaknesses in infrastructure such as telecoms, transport, ports, water and sanitation
11. Weaknesses in institutions e.g. government, civil service money and capital markets
12. Relatively higher tariffs and other import controls
13. Tendency to have capital controls / relatively closed capital markets
14. Lower access to advanced (rich) country markets because of trade barriers

### **Human Capital and Economic Development**

- Human capital is a critical component of understanding development economics. It is a repository of skills and health that can be used for economic activities
- Human capital is the capital that is in human beings rather than in machines. It encompasses physical, emotional health; educational knowledge, skills and experiences.
- Better human capital empowers people to make more of themselves
- Human capital is a measure of economic development, with better education and health, people can become more productive and competitive, both of which drive long term economic growth for example through faster innovation and an increased ability to adapt to and make good use of new technologies.

## Measuring Development

### **Amartya Sen on measuring development progress**

- The world economy has changed radically over the last thirty years. In a world of one priority (e.g. a focus on reducing extreme poverty measured by GNI per capita below \$1.90 a day PPP) you miss out a lot of things – we need to take again a wider view on a range of issues like climate change, human development, and nuclear energy.
- The problem of development and the deprivation of human lives remains the central issue. Sustainable development must include everything that human beings value.
- Measurability in human development is basically a process of ranking i.e. A is better than B and B is better than C.

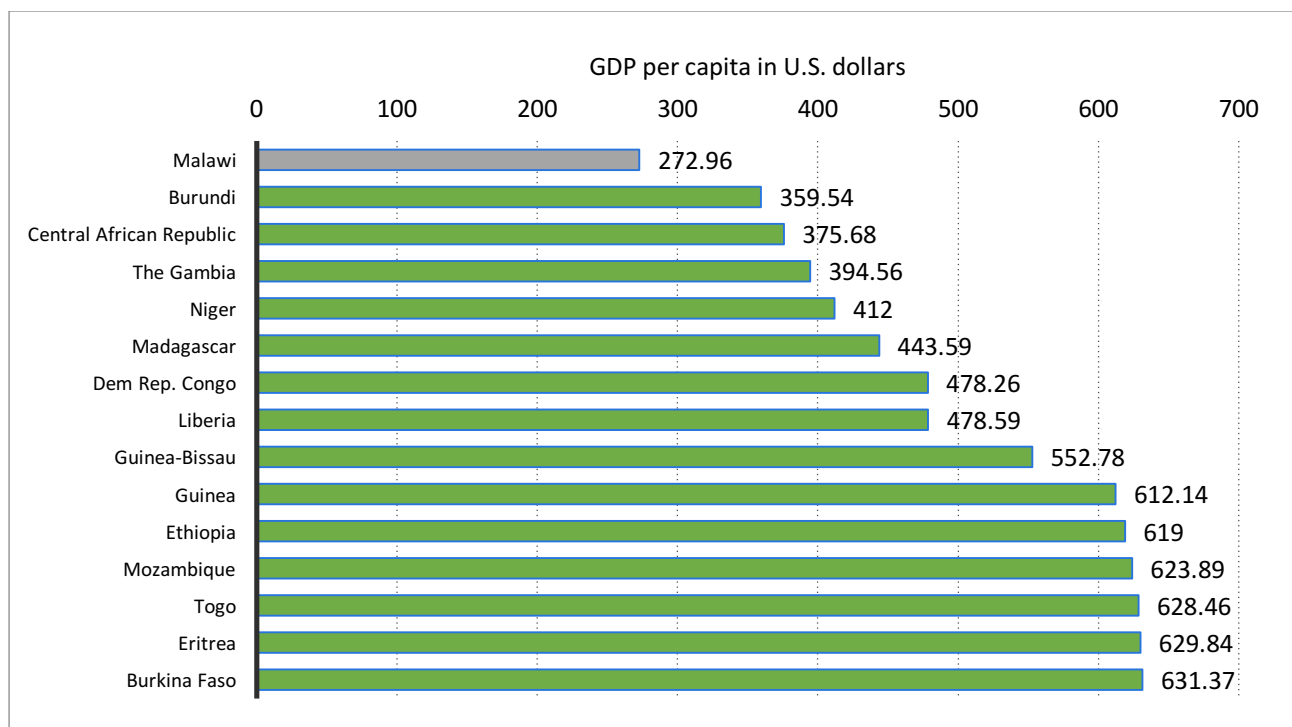
### Measurement methods

There are many ways of measuring the extent, durability and progress of improvements in human economic development. Some of the key development metrics are summarised below:

- Changing structure of national output, trade and employment
- Risk of extreme poverty – % of pop living on less than \$1.90 per day (measured at PPP)
- % of adult male and female labour in agriculture, % of arable land that is cultivated
- Combined primary/secondary school enrolment figures
- Access to clean water / improved sanitation facilities
- Energy consumption per capita / depth of hunger, incidence of malnutrition

- Fertility rates, natural rate of growth of population
- Prevalence of HIV, years of healthy life expectancy, child mortality
- Access to mobile cellular phone services, access to bank accounts, insurance
- Dependence of a country on foreign aid / levels of external debt
- Availability of /scope of social support through welfare programmes
- Unemployment and vulnerable employment rates, % of female population in paid work
- High-technology exports (% of manufactured exports), patterns of exports
- Degree of primary export dependence
- Changes in the published value of the Human Development Index (HDI)
- Progress in improving outcomes using the Multi-Dimensional Poverty Index (MDPI)
- Progress in achieving Sustainable Development Goals (MDGs)

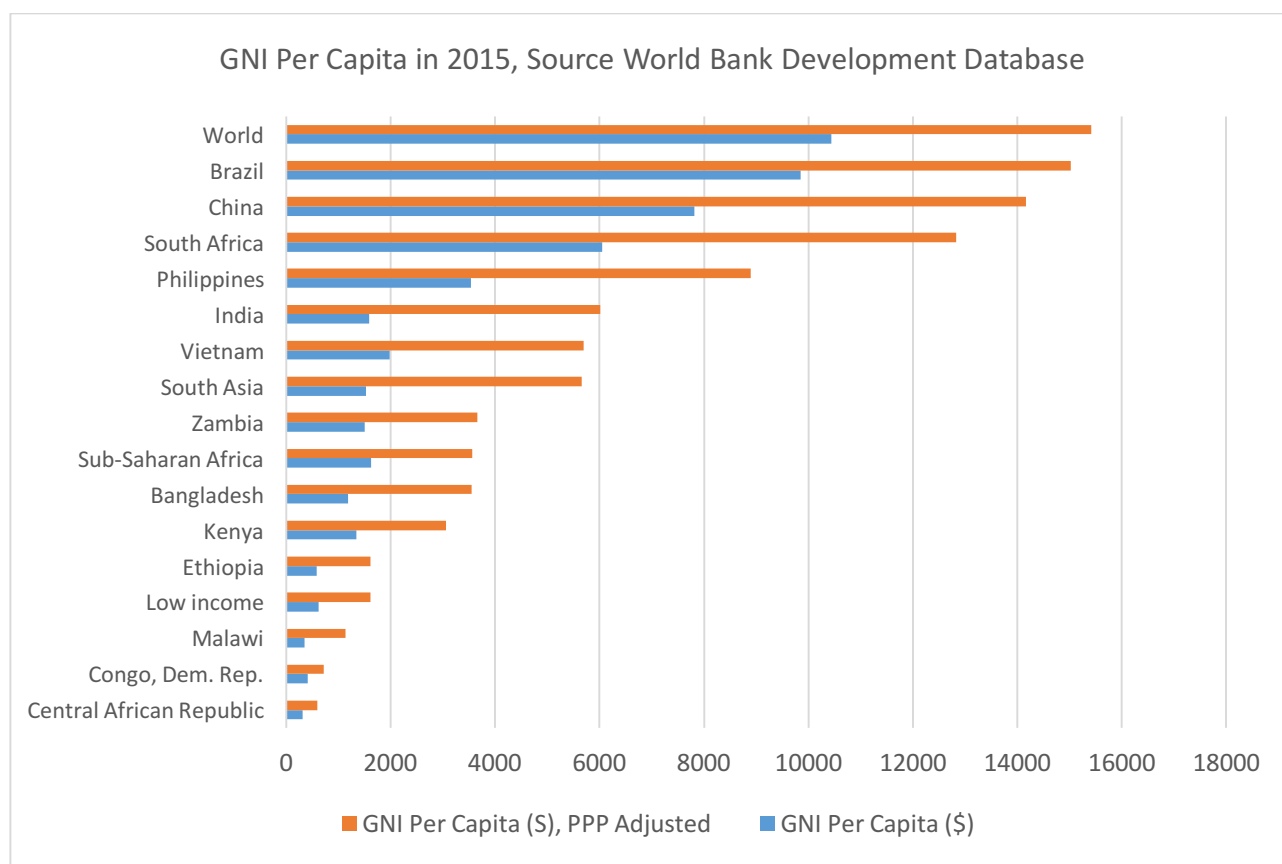
### Countries with the lowest (\$) GDP per capita in 2015



GNI per capita = GDP per capita plus net inflows of income for a country's people from overseas investments and remittances. Data for GNI per capita for a selection of countries – PPP adjusted is shown in the next chart.

### GNI Per Capita and GNI Per Capita (PPP Adjusted)





For the majority of developing countries, their PPP adjust GNI per capita is significantly higher than GNI per capita without the PPP adjustment. Consider for examples, countries such as Vietnam and India – where the GNI per capita PPP figure more than doubles.

	GNI Per Capita (\$)	GNI Per Capita (\$), PPP Adjusted
Central African Republic	320	600
Congo, Dem. Rep.	410	720
Malawi	350	1,140
Low income	620	1,611
Ethiopia	590	1,620
Kenya	1,340	3,060
Bangladesh	1,190	3,550
Sub-Saharan Africa	1,628	3,562
Zambia	1,500	3,660
South Asia	1,533	5,653
Vietnam	1,980	5,690
India	1,590	6,020
Philippines	3,540	8,900
South Africa	6,050	12,830
China	7,820	14,160
Brazil	9,850	15,020
World	10,437	15,415

### Share of GDP by Sector by Country (2014)

The table below shows the share of GDP by value added from each industry is shown in the chart below. Economically less-developed countries typically have a higher share of output from primary industries and manufacturing, although some countries are industrialising at a rapid rate.