Alternative theories of economic underdevelopment

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Outline

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  - Theory of dependence
  - Endogenous causes

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  - Exogenous technical progress (neoclassical growth theory)
  - Endogenous technical progress
  - New Institutional Economics

Different approaches to overcome underdevelopment and poverty

- Modernization and Dependencia theories:
  - For the proponents of Dependencia theory, the integration into world trade of developing countries is the main obstacle to development.
  - Modernization theorists recognize the increased world market integration, linked to the neoclassical growth theory, as the basis for development.

Modernization theories

- Under the preamble of the modernization theories a number of explanatory approaches for underdevelopment of developing countries and strategies to overcome them are summarized.
  - Various reasons such as lack of capital, lack of entrepreneurs, traditionalism, etc are placed in the foreground.
- All these theories are based on a process of imitation and adaptation to the western industrialized countries

Phase model

Walt Rostow (1960):
„Stages of Economic Growth“,
Cambridge University Press

-> 5 phases of development

Walt Rostow Geb. 1916

Rostow and the phases of development

- Third World countries need to get out of their state of Tradition to Modernity
- The path from tradition to modernity was, among others, developed in WW Rostow stage theory of economic growth.
- He divides the development process into the following 5 phases:

Rostow's 5 stages of development (modernization theory)

1. Traditional society
2. Start-up period to create the precondition for economic recovery
3. Economic boom ("take-off")
4. Maturity
5. Era of mass consumption

3 necessary conditions to achieve the "take-off“phase

- Increase productive investment to at least 10% of national income.
- Development of several industrial sectors with high growth rates.
- Creation of the necessary political, social and institutional framework.

Economic development can only take place through the growth of industry, but needs a leading sector.

Leading sectors

- Individual sectors need to evolve through the application of modern science and technology to the so-called leading sectors.

- Over time various industries occupy this position.

- Historically, in the industrialized countries, this task has been fulfilled by the manufacturing sector, propelled by the textile industry, the railway, the iron and steel industry, the chemical and electrical industry, automotive, information technology, etc.

Characteristics of a leading sector

- High income elasticity of demand
- Above average growth rate
- High elasticity of supply for short-term rapid growth in production.
- Creation and dissemination of technological improvements to other industries.
- The agricultural sector lacks these features, so it cannot be the leading sector.

Economic policy

- Integration into the world economy is considered indispensable
- Lack of development factors such as capital and know-how can be introduced in exchange for products with comparative cost advantages.

The dependency theory

- The "neo-colonial dependency model": Developed the mid-60s in Latin America
- Response to the failure of the world market integrative development model of most Latin American countries.
- Centuries of dependence of developing countries from developed countries prevented their development.
- The developed relationship between colonial raw material suppliers in the developing world and the industrialists in Europe today still exist: The former colonies can only evolve if the circuit is broken

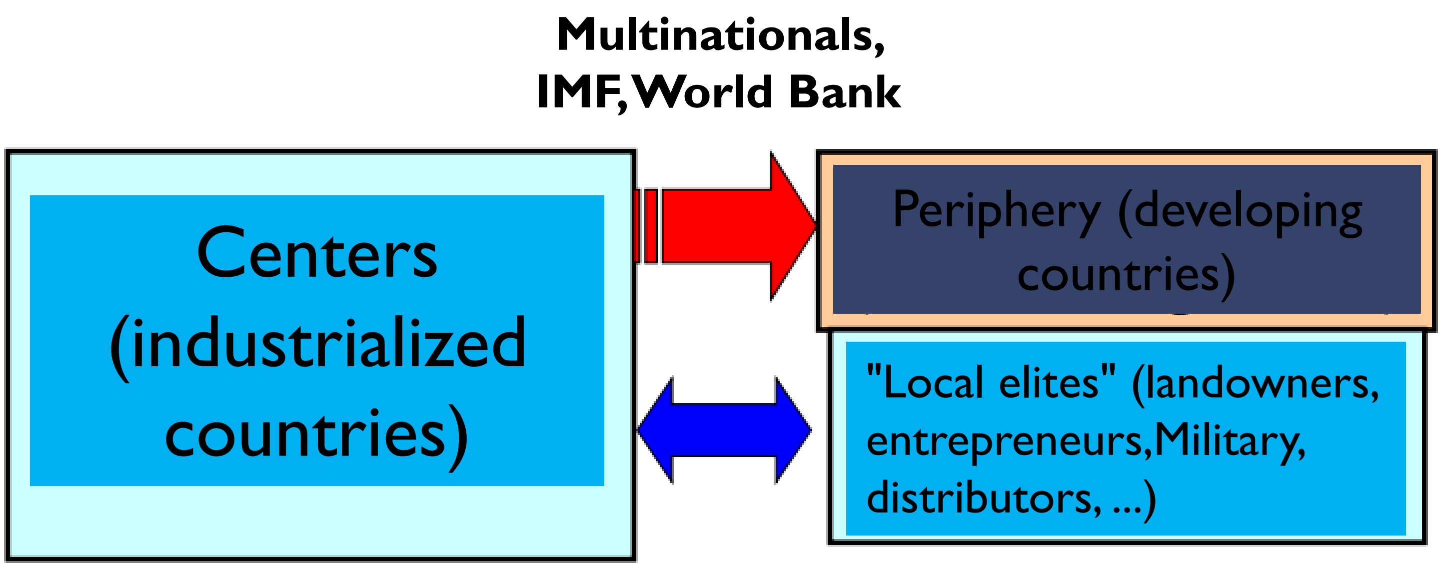
The dependency theory

- There is no general theory for overcoming underdevelopment

-> Each country must develop a specific development strategy

The dependency theory

- The "neo-colonial dependency model,,:



The dependency theory

- Theotonio Dos Santos, (1970), „The Structure of Dependence", The American Economic Review, 82, S. 231-236.

- Emphasizing the balance of power:
  - „dependencies"
  - "interests"
  - "influence„
  - "power"

The dependency theory

3 forms of dependency (Dos Santos):

- Colonial dependence:
  - "With the help of a trade monopoly supplemented by a colonial monopoly of a country, mines and labor."
  - Colonial development of the countries resulted in very adverse conditions today
- Financial-industrial dependency:
  - "Characterized by the predominance of large capital of the hegemonic centers"
- Technological-industrial dependency:
  - "Having regard to multinationals ... technological monopoly of the imperialist centers"
  - Developing countries depend technologically on the industrialized countries and on their willingness to sell high technology

The dependency theory

- Dos Santos (1970):

Argued that "the dependence of Latin American countries from other countries can not be overcome without a qualitative change in their internal structures and their foreign relations."

- Institutional reforms: revolution, expropriation

- Dissociation approach (auto-centric development) of Senghaas (1978):

- Development of the internal market potential by increasing the balance between agriculture and industry. Foreign trade should have a complementary role.

Protectionism and falling "terms of trade"

- The protectionism of developed countries implies that the developing countries are unable to effectively sell their products on the markets of developed countries.
- Raul Prebish and Hans Singer argued that developing countries normally export primary products and import manufactured products.
- The prices of the primary products in relation to the manufactured products have declined over time, leading to falling "terms of trade“.

Modernization theory vs "dependence approach "

- The comparison of these two groups of developing strategies for the developing world, shows that in addition to the well-known difference in the sectoral priority especially the foreign trade regime is different.
- On the one hand, the integration into the international division of labor is a prerequisite for development, on the other hand it is the obstacle.

Endogenous causes of underdevelopment

- Economic order:
  - Unclear economic system with central banks which are not independent.
- Low propensity to save:
  - propensity in developing countries: very low; propensity in industrialized countries: saving rate 12% to 20% of income
- "Bad governance" and corruption:
  - Unstable political situations without functioning democracies;
  - Corruption
  - Inefficient institutions such as the legal system and property rights

Growth theoretical approaches

- The classical dynamics of Adam Smith and Malthus
- Exogenous technical progress (Neoclassical Growth theory)
  - Robert Solow: Absolute convergence -> Catching-up hypothesis
- New Institutional Economics
- Endogenous technological progress (new growth theory): Conditional Convergence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