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Alfred Maizels', Exports and Economic Growth of Developing Countries: A Review Article

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Alfred Maizels' Exports and Economic Growth of Developing Countries: A Review Article

Although the title and sub-title of this book[1/] suggest that it is a study of the theoretical and empirical relationships between exports and economic growth, the book is primarily devoted to projecting the level of imports, net capital flows, exports, and gross domestic product in 1975 for 5 developed and 18 less developed, overseas Sterling area countries. These projections are based on a modified Chenery-Strout macro-economic growth model (American Economic Review, September 1966) applied to the base period of 1960-61, with the capacity to import taken as the effective constraint on economic growth. The export projections for individual countries are based on detailed commodity projections which are discussed in a 146-page appendix, and also on an analysis of trends in world trade, demand, population growth and assumed changes in the shares of selected countries in this trade.

The major modification of the Chenery-Strout model is that the study projects the prospective trade gap for a given rate of economic growth for a country, and deducts this from the projected investment required to support the output target, to derive domestic saving as a residual. The trade-constrained growth assumption is then tested by comparing the derived savings, with the savings that results when the past relationship between savings and income is projected to the target year.

1/ Alfred Maizels, assisted by L.F. Campbell-Boross and P.B.W. Rayment, Exports and Economic Growth of Developing Countries: A theoretical and empirical study of the relationships between exports and economic growth, with illustrative projections for 1975 for the main overseas Sterling countries, Economic and Social Studies Series of the National Institute of Economic and Social Research, Cambridge University Press, 1968.

This trade-constrained growth model is then used in two ways. On the basis of a projection of exports, capital flows and certain specific parameters, the model is used to determine the probable rate of economic growth of each country. In addition, the model is used in reverse to determine the amount of net capital flow that would be required to support a given target rate of economic growth, on the basis of a projected growth rate of exports.

The model is based on the hypothesis that fixed capital investment is the dynamic element in economic growth and that in the case of the less developed countries the level of investment is largely determined by the capacity to import. Hence, the foreign exchange availabilities constitute the effective restraint on economic growth. The degree to which foreign exchange can be transformed into capital assets is taken to depend on the country's incremental propensity to invest with respect to the capacity to import, while the degree to which an increase in capital assets can be transformed into additional output is taken to depend on the incremental capital-output ratio.

The general conclusions reached by the study are not encouraging. For the majority of the less developed overseas Sterling area countries, the projected export and economic growth rates fall short of those contained in the country development plans. On even the most favorable assumptions, the projections indicate that there would not be any dramatic improvement in per capita real income in the majority of the countries by 1975. At the rates projected, Burma and Pakistan

would not achieve a per capita income of £100 until the middle of the next century, and for Ceylon and Kenya, it would be in the early part of the 22nd century. The study concludes that if the countries are to reach a growth rate of 5 per cent in real gross domestic product, or 2-1/2 per cent in per capita product by 1975, the countries will need both larger amounts of foreign aid and a faster rate of growth in exports. Even under the most optimistic assumptions, a doubling in the net flow of official capital would be needed by 1975 to reach the 5 per cent target.

The study recommends four policy measures for the LDC's to deal with the problem. These are to increase the competitiveness of traditional exports, to diversify exports in favor of 'dynamic' commodities, to expand the volume of intra-regional trade among the LDC's, and to expand exports to the Communist countries. It is also suggested that the industrialized countries reduce their tariffs on manufactured goods and substantially increase the level of their foreign aid.

Much of the argument in this book is based on the notion that the key to expanding growth in the less developed countries lies in the injection of large amounts of capital. It is even assumed that the rate of growth can be pretty accurately predicted if one only knows the amount of capital available for investment and the incremental capital-output ratio. It is recognized that human capital is also of some importance, but this does not get much attention since it is not easily quantifiable.

It is now recognized much more widely than it was a decade ago that all of the factors that influence the productivity of capital can in turn be influenced by the prevailing system of economic organization—the laws, regulations and policies that impinge upon man's economic decisions. Of perhaps greater importance than the quantity of capital are such considerations as the incentives provided for economic effort, the stimulus to inventiveness and imaginative enterprise, freedom to buy and sell in the most advantageous markets, and the freedom of capital to find its way to those most competent to employ it efficiently.

This adds up to market freedom, encouragement of private entrepreneurship and avoidance of the distortions caused by inflation and unrealistic exchange rates. It places emphasis on education and development of people with talents that can contribute to raising the level of productivity.

Maizels misleads in suggesting that the proper policy is to focus on increasing foreign aid rather than on developing domestic policies which will be conducive to more efficient use of the resources already available to the developing countries. This, if properly done, will tend to attract private capital and know-how from abroad. It is also no service to reinforce the already strong tendency of the developing countries to look to changes in the trade policies of the developed countries to expand their export prospects. While more liberal trade policies, both in the developed and developing countries are desirable, it is not valid to assume that many developing countries could not

achieve more rapid export expansion even under present conditions. Nationalist China and Korea have in recent years achieved very high rates of export growth, accompanied by high rates of GNP growth. Most of this has been as a result of expanding sales of manufactured products to industrialized countries. Other countries with equally good physical endowments have lagged far behind. A few, such as Burma, have even suffered serious declines in their strongest traditional exports. Burma is currently faced with abysmal prospects for rice exports, chiefly because of the inflexibility of official price policies.

Doubts regarding the validity of the assumptions underlying the model used in Maizels' study are confirmed by the results of the regression analysis contained in Chapter One—results which the author evidently does not accept. The regressions of GDP on the capacity to import did not show the significant statistical results expected. However, regressions of GDP on export volume showed significant results (p. 49). The first result is not surprising, since if a country merely receives foreign aid, or has foreign exchange available, this does not guarantee a substantial rate of economic growth. On the other hand, there is a logical explanation, rooted in the theory of comparative advantage, which explains why high rates of export growth lead to high rates of economic growth. If a country can expand its exports, competing successfully in international markets, it is producing efficiently by specializing in those products in which it has a comparative

advantage, and it is thereby increasing its productivity. This increase in productivity, which is the essence of development, leads to an increase in the rate of economic growth.

Although the book's projections are detailed and internally consistent—and for this reason may be of interest to economic planners—they are based on many assumptions (some of them dubious as indicated above) and on such fragile parameters as capital-output ratios and investment elasticities. Long-term forecasts have often been wide of the mark in the past, and the better part of caution would suggest that not too much reliance be placed on the validity of these projections.