Chapter 9: Economic Development, Growth and Capital Formation

The concept of economic development is dynamic and multidimensional. With the passage of time, this concept is evolving. As this concept relates to developing countries, they are still suffering from poverty, hunger, unemployment, inequality, inadequate socioeconomic infrastructures, etc., but developed countries don't have these problems since they have already resolved these issues.

As a synonym for economic growth, economic development is used. Nevertheless, both are different from each other. Economic growth is measured by the increase of the country's GDP.

Meanwhile, a country's economic development typically means an increase in its citizens' quality of life. The human development index (life expectancy, literacy rate, and poverty rate) determines what quality of life a person can expect. Thus, economic development involves the increase in the standard of living of the people of a country from a low-income to a high-income status.

Characteristics of Developing Countries

A developing country is a country with a less developed industrial base and a low Human Development Index (HDI) relative to other countries. Developing countries tend to have some characteristics in common often due to their histories or geographies. For example, with regards to health risks, they commonly have: low levels of access to safe drinking water, sanitation and hygiene; energy poverty; high levels of pollution (e.g. air pollution, indoor air pollution, water pollution); high proportion of people with tropical and infectious diseases (neglected tropical diseases); a high number of road traffic accidents; and generally poor infrastructure.

Following are the major characteristics of developing countries.

i) Low per capita income:- The per capita income of developing countries like Nepal is very low. The per capita income of Nepal is us dollar 766 which is very low as compared to it's neighboring like India, china and Pakistan.

ii) Mass poverty:- There is mass poverty in developing countries like Nepal. About 22% of total population of Nepal is below poverty line. Mass poverty is due to low per capita income and unequal distribution of income.

iii) Excessive dependence on agriculture sector:- agriculture sector is regarded as the backbone of Nepalese economy. About 66% of total active population of Nepal is engaged in agriculture farming. About 32% of total GDP of Nepal has contributed by agriculture sector.

iv) Underutilization of natural resources:- Nepal is very rich in natural resources like water resources, forest resources and mineral resources. There is no proper utilization of these natural resources. Nepal has about 6000 rivers which have potentiality of generating 83000 Megawatt of hydroelectricity, but Nepal has able to generate only 830 megawatt hydroelectricity. This data shows that there is underutilization of natural resources.

v) High trade deficit:- Trade deficit occurs when the value of countries import is greater than the value of countries export. And in context of Nepal, there is high trade deficit because Nepal imports more and exports less. Therefore, Nepal should produce those goods and services which have comparative and competitive advantage.

vi) Rapid population growth:- there is rapid population growth in Nepal. According to population census, population growth rate of Nepal is 1.4%, this is higher than other developed countries. The main reason for rapid population growth in Nepal is illiteracy early marriage, polygamy etc.

vii) Remittance economy:- There is lack of employment opportunity in Nepal. Therefore, large number of Nepalese youths has migrated to foreign country in search of job. They have gone especially to Malaysia, Qatar, and Dubai etc. The money earned by these peoples are sent to Nepal in the form of remittance. Remittance helps to improve the living standard of people and reduce poverty.

Indicators of Economic Development

An economic indicator is a statistic that measures economic activities such as unemployment rate, industrial production, literacy rate, standard of living etc. Economic indicators help to analyze the economic performance and prediction of future performance of a country. The measures indicators of economic development are explained below:

Per capita income (PCI) or average income measures the average income earned per person in a given area (city, region, country, etc.) in a specified year.

It is calculated by dividing the area's total income by its total population. Per capita income is national income divided by population size.

Physical quantity of life index:- It consists of three indicators, they are:

- Life expectancy
- Infant mortality rate
- Literacy rate

Human development index:- Human development Index (HDI) was introduce by UNITED NATIONS DEVELOPMENT (UNDP) in 1990. According to this criteria economic development is evaluated on the basis of following:

- GNI per capita
- Education Index
- Life expectancy at birth

Process of Capital Formation

Capital formation is the process of increasing the stock of real capital in the economy. Capital formation involves making more and more capital goods. It is defined in both narrow and wider sense. In the narrow sense, capital formation means the expenditure made on fixed capital such as plants, machinery, tools etc. In the broader sense, capital formation is the investment in human capital along with material capital.

The process of capital formation are explained below:

i) Creation of saving

ii) Mobilization of saving

iii) Investment of saving