

The new strategy of economic growth

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Abstract:

This paper aims at exposing actual economic growth strategies, in quest of a new one for the future decades. By analyzing strength and weakness related with it according to a literature review. The findings show that even helpful actual strategies seems insufficient to realize promises of development as reducing poverty and realizing catch up with progress. However, the study points that in the nexus between growth, poverty and employment will hold answers to policy maker on how to sustain economic growth.

Keywords: Economic growth, employment, social cohesion, inclusive growth, poverty;

ملخص:

تهدف هذه الورقة إلى عرض استراتيجيات النمو الاقتصادي الراهنة، سعياً لاستراتيجية جديدة للعشريات المقبلة. من خلال تحليل نقاط القوة والضعف المتعلقة بها التي وفقاً للأدبيات حول الموضوع، وقد أظهرت النتائج أنه رغم كون الإستراتيجيات الحالية نافعة إلا أنها بدت غير كافية لتحقيق وعود التنمية كالإقلال من الفقر والمضي قدماً. أشارت الدراسة تبعاً، أن التشابك بين النمو، الفقر والتشغيل سوف يحمل إجابات لصناع القرار حول كيفية تعزيز النمو الاقتصادي.

الكلمات المفتاحية: النمو الاقتصادي، التشغيل، التماسك الاجتماعي، النمو الإحتوائي، الفقر.

Introduction:

Recently a great attention had been given to develop a new economic growth theory based on social welfare; essential subjects treated are employment and poverty in a nexus with production process.

The famous premier model of Robert Solow established a rule according to which production is a function of both capital (K) and labor (L), even useful as a mechanic tool for the estimation of output i.e. gross domestic product (GDP) in an economy; it couldn't explain at least the well known Solow residual which represents others factors productivity; moreover it can't fulfill promises of treating well being matters as equity, employment, poverty and inequality, it's certainly hard to quantify such variables but it's necessary at least take them with projections to identify how promising growth is.

The early works on economic growth models doesn't integrate or consider key elements in production function, which are mostly qualitative; it was just in modern theories where models introduced the human capital as a factor of production, this could be reconsideration of classical or exogenous growth theory assumptions.

The present work is an essay to find an answer to the following problematic: **How strong is the actual strategy of economic growth? And what are essential characteristics of the new substitute for it?** By identifying aspects of the new growth strategy, and analyzing characteristics of existing growth models in order to give prominent guidelines for policy makers of both developed and developing countries.

Methodology and experimental procedure

The paper contains 4 sections; the first one is about motivations of our assumption, and the second one is devoted to describe the new growth strategy, while section number 3 treats differences between the old and the new economy according to a literature review, in final section a discussion of the fundamental matter about the nexus between growth, employment and poverty was implemented.

First. In quest of a sustained growth

Traditionally to increase the rate of GDP growth, it's necessary to make a choice between the extensive (adding supplementary quantities of factors) and intensive (better using of factors i.e. productivity) policies, or merge the two factors in a single strategy, these are not a sufficient criterions to consider growth sustained according the IMF definition "having at least a 7%

permanent growth rate for a decade or more”, growth boosted by primary resources booms of prices or by a recovery from past collapses are excludedⁱ. In another words a faster growth rate could occurs as a response to volatile elements i.e. inflation, booms in the market of some good especially food and primary resources.

In earlier description of production process, researchers incorporate just material or tangible factors, namely capital (K) and labor (L), with a consideration of variables as exogenous, and when this model fail to describe the growing GDP with an invariant quantities of factors they reconsidered suppositions by introducing technological progress (T) as a factor of production, surprisingly experience of some countries shows that even in a stable quantities of K, L and T had seen their GDP growing up rapidly, then came the second generation of economic growth models namely the endogenous models.

Various findings are obtained according to empirical researches on economic growth sources; some essential findings could be summarized as follows:

I. That human capital can be main factor to explain slow growth of resource-rich countriesⁱⁱ, policies such as: learning, expending on investment in R & D, reforming education system, represents a promising tools for the new paradigm of knowledge-based economy;

II. Gylfason (2001) cited 4 channels of transmission from abundant natural resources to sluggish economic growth: the Dutch Disease, rent seeking, government mismanagement, and low levels of human capitalⁱⁱⁱ;

III. Some potential factors had a controversial effect on growth according to empirical studies, like openness on foreign trade, democracy, foreign direct investment, factor liberalization...etc.

Moreover topics of the agenda for sustained growth are supposed to be:

- Regarding macroeconomic policy by looking beyond frontiers of stabilizing pacts which restricts intervention of governments on markets orientation, and working with a certain degree of coordination and integration with exterior fluctuations;

- Regarding economic reforms priorities should be selected in accordance with goals (more production, more competitiveness, qualified entrepreneurial activities...);

- Regarding employment policies; a coherent golden pillars for the labor market should be undertaken with the right (not intuitive) decisions by an effective mixture of financial policies at long run.

- Regarding social protection defined as ‘the public actions taken in response to levels of vulnerability, risk and deprivation which are deemed socially unacceptable within a given polity or society’^{iv}.

Lundvall mentioned that: "‘Know who’ is becoming a critical competence in economic contexts in contrast to ‘know-why’, ‘know-what’ and ‘know-how’"^v; which means that the best way for organization to be more competitive is to access knowledge rooted in different disciplines; the main way to achieve such objective in developing countries could be attained by social contact from the leaders and managers to the bottom (employees); using a dynamic environment by incorporating connections between job creation and employee’s function in the society.

Focusing only on physical and/or human capital is not sufficient. According to the new economic theory; it’s necessary to understand “why societies differ in the efficiency with which they use their physical and human capital” more than understanding the process of sustained economic growth or accounting for large cross-country differences in income.

Second. The new growth strategy

New strategies are based on the concept of maintaining growth rate above 6% per year for at least a decade of time. Here are some proposed strategies.

I. 1st strategy: Islamic finance as a source of growth

While the Islamic financial model proposed various tools to boost investment in order to mitigate stagnant growth, theory still lack for socio-political bridges to transfer recognition of Islamic civilization principles, in such substitute Islamic model there is a necessity for more than financing modes. To build such thrived model, multi-disciplinary functioning, innovation, and efficiency are strategic instrument to sustain outputs of the model and guarantee their continuity.

II. 2nd strategy: inclusive growth

The IG refers to both the pace and pattern of growth, which are considered interlinked,^{vi} as a process it can be characterized as broad-based growth that includes nondiscriminatory participation (i.e. minimum rate of unemployment), in addition it benefits many people (i.e. the poor, middle income groups and even the rich^{vii}) if seen as outcomes of the growth process. The last point of view is closely related to the much-discussed concept of PPG^{viii}, which treats the interrelation between growth, poverty, and inequality^{ix}.

Different measures are proposed to identify whether growth is pro-poor or not (i.e. anti-poor or pro-rich), disparities in general are related to unconventional views about the aspects of poverty and how it can be measured using a threshold to separate poor from well off people (especially absolute and relative sense of poverty).

In fact there is no consensus on how to define PPG or IG, and even both concepts are interconnected and used interchangeably in poverty eradication literatures to indicate the same meaning; differentiation between them is of necessity (see tab.1).

Tab. 1 Differences between PPG and IG concept

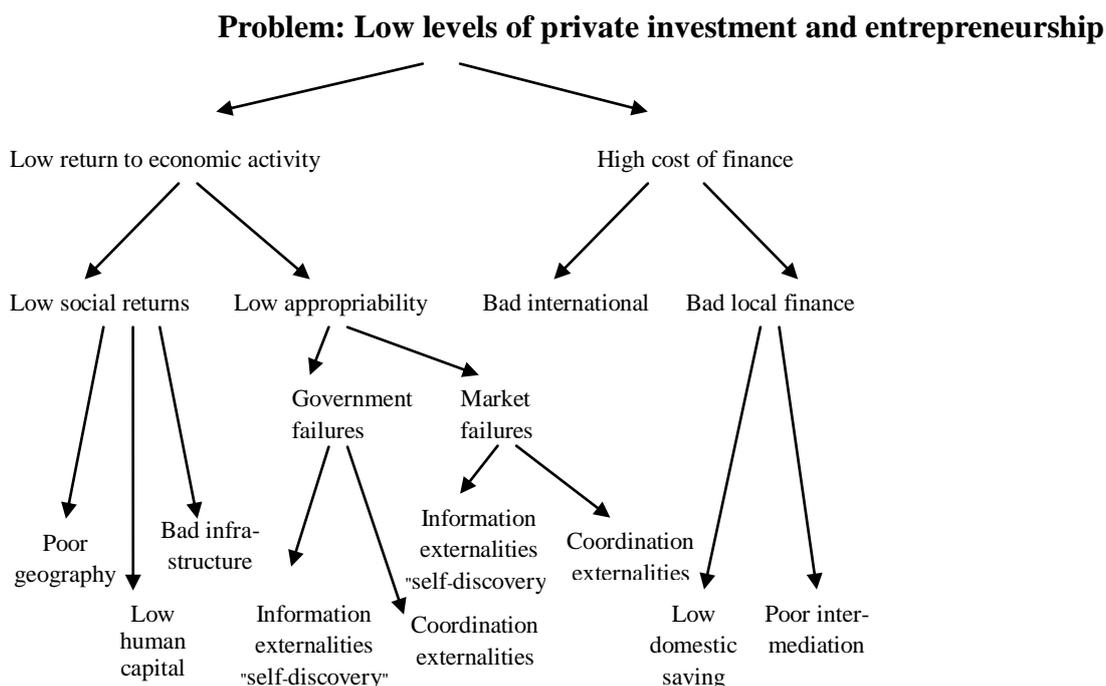
Criterion	PPG	IG
Benefits	The poor	All people
Potential outcomes	Distributive change and/or real income rise up	Broad based across sectors, more productivity, new jobs
Interval	Short run	Long run
Determinants	Macro policies (growth rate boosters, distributive policy)	Interlink between micro and macro determinants
Interests	Welfare of the poor	Opportunities for the majority of the labor force
Hindrances	Income Inequality, stagnation, recession	Inequity, asset inequality of opportunities, unprotected jobs

Source: Author; Using different sources.

III. 3rd strategy: Remove constraints to economic growth

Hausmann, Rodrik, and Velasco developed a framework to capture growth constraints in the short-run, using a decision tree (as in Fig. 1).

Fig. 1 Growth diagnostics



Source: Hausmann, R., D. Rodrick, and A. Velasco (2005) Growth Diagnostics. John F. Kennedy School of Government, Harvard University.
<http://ksghome.harvard.edu/drodrik/barcelonafinalmarch2005.pdf>

This strategy was criticized by its reformist charter in short run level, and omission of fundamental restructuring of the production model in the long run, concerning labor market adjustment, productivity stimulus, capital accumulation...etc.

IV. 4th strategy: Inputs or growth process strategy

A high attention increased with the negative impact of financial crisis on corporations as well as economic growth, which lead to severe consequences for employment and social inclusion. With budget constraints putting pressure on national education and social policies, there is a need to optimize efficiency and results of the education and training systems, providing the skills demanded by the labour market, and at the same time preventing social exclusion and poverty.

Policy approach proposed as remedy is flexicurity derived from the successful models in the Netherlands and Nordic countries; it attempts to combine flexibility of labour markets for employers and security of employment for employees as a key element of European Employment Strategy. All members in European Union were appealed to enlarge flexicurity application. Education and training are supposed to have a vital role in providing a sense of security for workers, and sufficient skills to build the ability to find a new opportunity in labor market.

Flexicurity requires an integrated approach to enhance both flexibility and security in labour markets rather than ad hoc measures/actions which promote either one or the other probably at the expense of both. This integrated approach invites policy makers to take concerted action to ensure:

- Sufficiently flexible contractual arrangements;
- Comprehensive lifelong learning (LLL) strategies;
- Effective active labour market policies;
- Modern social security systems.

However, there is not a unique model for or to flexicurity. The balance between flexibility and security and the policy options towards flexicurity is the negotiated outcome between governments and social partners and depend on specific national contexts - namely the specific labour market challenges- that each country is facing and its institutional setting.

The vague literature on this subject except for some European economies (EU 2020 strategy for growth and jobs), hide evidences on how flexicurity will be performed for developing countries, and what will be their potential effect on social cohesion, poverty and inequality.

In the other hand establishing such policy necessitates support more than aid from EU. As example between many programs there is the 23.5 million euro Youth-Employment Support Program which has been approved by the European Commission in 2012.^x

Third. The new and the old economy

Audretsch and Thurik (2000) mentioned that due to comparative advantages from using labor especially in Asia and benefiting from the technological revolution; a shift had been emerged from the managed economy toward the entrepreneurial economy, characterized by a 14 trade-offs^{xi} (see tab .2).

Tab. 2 Trade-offs between managed and new economy

Forces underlying managed versus entrepreneurial economy				
Managed	Globalization	Continuity		Jobs or high wages
Entrepreneurial	Localization	Change		Jobs and high wages
Differences in the underlying environment				
Managed	Stability	Specialization		Homogeneity
Entrepreneurial	Turbulence	Diversity		Heterogeneity
Firms functioning				
Managed	Control	Firm transaction	Competition and co-operation as substitutes	Scale of output
Entrepreneurial	Motivation	Market exchange	Competition and co-operation as complements	Flexibility
Government policy				
Managed	Regulation	Targeting outputs	National policy	Low-risk capital
Entrepreneurial	Stimulation	Targeting inputs	Local policy	Risk capital

Source: David B. Audretsch and A.Roy Thurik, what's new about new economy? Sources of growth in the managed and entrepreneurial economies, Institute for Development Strategies IDS, USA, 2000, p. 6-28.

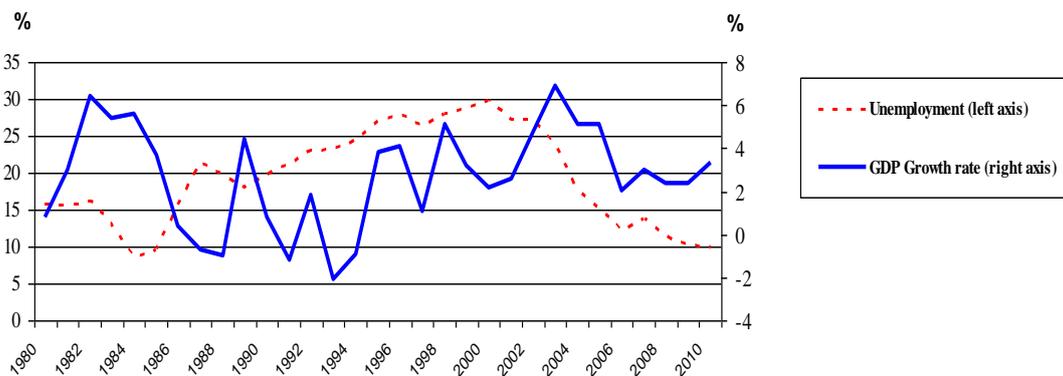
What seems to matter for sustained growth is whether manufacturing exports rise as a share of total exports during the growth spell. A one percentage point increase in manufacturing exports is associated with an increase in the expected duration of a growth spell by 3 to 6 per cent^{xii}.

Fourth. The nexus between growth, poverty & employment

Pro-poor versus sustained economic growth

While economic growth and employment looms as a major challenge for European countries and the west, developing countries are experience this dilemma in a nexus with poverty, Algerian economic structure characterized as oil rental is the source of vulnerability to exterior chocks -driven by barrel prices fall down- inducing public investment reduction, less production and more unemployment (Fig .2).

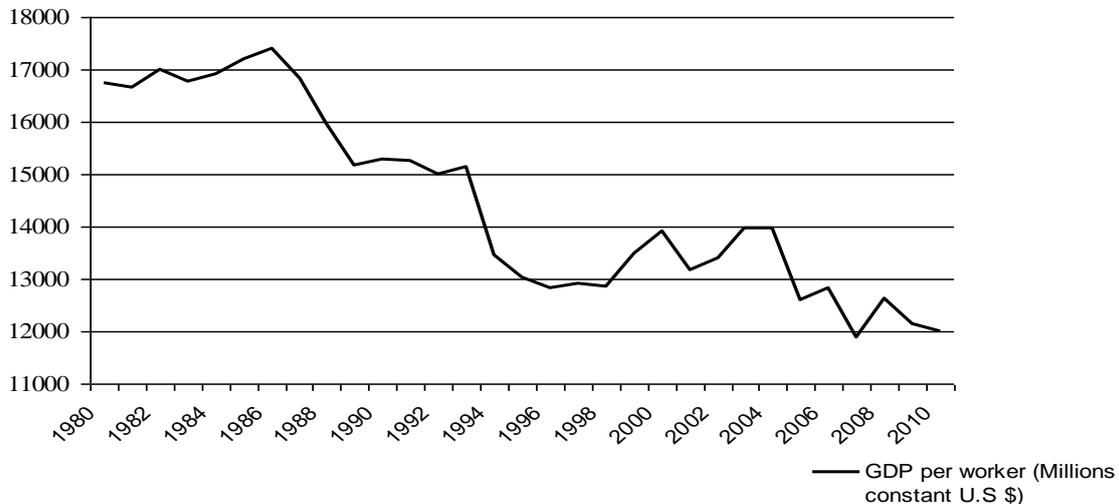
Fig.2 Economic Growth rates and unemployment during 1980-2010 in Algeria



Source: National office of statistics. At: www.ons.dz

Even more productivity per worker experienced a continuous decrease as seen in figure number 3.

Fig 3. GDP per worker during 1980-2010 in Algeria



Source: author calculation using national office of statistics.

A newly emerging economy in Europe termed as the entrepreneurial economy^{xiii} were experienced by 3 countries: Netherland, Denmark and U.K, as a long run strategy to palliate the unemployment effects on social cohesion, the idea of this strategy is to empower social asset by knowledge including improving educational systems, encourage training in a way to support small businesses and innovation.

As the OECD points "the failure of continental European countries to adopt its recommendations reflects their fear of increased earnings inequality. The question is whether it is possible to deregulate without suffering these malign effects". To reap gains from such strategy oriented in term of greater competitiveness, faster growth rate, and ultimately increased employment demands, developing economies must submit a loss, or at least a perceived loss of certain other economic policy goals.

Conclusion:

Economic situation of numerous countries over the world including -the Algerian economy- is characterized by an economic slow down with growing number of unemployed force of labor, while reasons re divergent a single strategy is proposed to fulfill in the gap:

- Promoting knowledge by an educational strategy, based on a long life training of individuals (essential methods required to be built in accordance with social cohesion principal);
- After building the basic needed social assets, flexicurity could be introduced in order to build a fair environment for both employers and employee without involving supplementary cost for government budget.
- Special focus has to be given to rising productivity en encouraging small firms, to build a broad based economy.
- Social costs need to be twin analyzed or discussed: first by researchers to build coherence between theoretic and empirical framework, second by coordination between policy maker and politicians.

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