

Theory of supply

Capital accumulation important at outset of development

Technological change (TFP) important after that

Productivity Slowdown in 70's

Conditional Convergence

GDP *levels* and GDP *growth rates*

TFP is main source of income differences across countries (and note how higher A causes higher K .)

Property Rights

Human Capital

Health

Political Stability/Wars

Openness to Trade/Ideas

Rule of law/Contract Enforcement

Competition/Deregulation/Gov

To start a business:

- U.S.: 5 days, 1% of average income
- Peru: 72 days, 33% of average income
- Haiti: 203 days, 127% of average income

Experiments: Korea, Germany, Hong Kong

Politics/Economics

Foreign Aid

How is TFP measured?

$$Y = AK^{\alpha}L^{1-\alpha}$$

Growth accounting and how to measure TFP
growth rates

Other Growth Theories

Malthus:

Rising incomes would lead to a higher population growth, so $\frac{Y}{L}$ would fall.

Malthusian Trap

Eventually, Y growth high, while L growth fell.

New Growth Theory:

What determines growth in A ?

Recipes and resources

Positive Externalities

Population

People as resources (human capital)

Incentives and Monopoly Power

$$S = I$$

i nominal interest rate

r real interest rate

Real Interest Rate = Nominal Rate - Inflation

$$r = i - \pi$$

Fisher Effect: to compensate savers and to ensure a given real return, nominal rates are higher in high inflation economies.

Loanable Funds Theory.

Assume 1) no inflation 2) economy always at potential 3) closed economy

Supply of Loanable Funds (households, government)

$$S(r) = a + br$$

$$I(r) = d - cr$$

Demand for Loanable Funds (investment)

Depends on Interest Rates

Slopes depend on elasticities

What shifts the curves?

Path to Equilibrium

In equilibrium, S , I and r change.

Shifts in Curves

Burden of adjustment

Examples:

Greater Budget Deficits and Crowding Out

Long-Run Effects

New technology in future

Taxes on investment

Recession and uncertainty

Inelastic