ECON 333 PROBLEM SET # 3

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Harrod-Domar model of economic growth and development was one of the earliest attempt to give a theory of development. They showed *"under certain assumptions"* that the growth in total output, $\frac{\triangle Y}{Y}$ which we denote as g_Y, is given by

$$g_Y = v \cdot s$$

where s is the saving rate, and v is the output-capital ratio.

1. Derive the above formula.

2. Currently India has a savings rate of 20 percent, and the annual growth rate in total output is 4.0 percent per year. First compute what is the value of output-capital ratio. Assuming that the output-capital ratio does not change over time, solve the following problem.

3. India would like to increase its growth rate of total output from 4.0 percent to 6.0 percent per year, what should be the corresponding savings rate? Recommend three important policies that might help India to increase its savings rate.

4. According to Harrod-Domar theory of economic development, *the main development concern is to understand how a less developed economy with low savings rate could be made to have a high savings rate, because then the economy will have a sustained high growth and hence development.* Briefly provide the strengths and weaknesses of this view of economic development in the light of economic development processes of the concurrent less developed economies.