AN OPERATIONAL DEFINITION OF ECONOMIC DEVELOPMENT: A FALSE HOPE*

by

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One of the problems facing those who work in the field of community development and its more general counterpart, rural development, is a lack of consensus concerning just what the terms actually mean. Economists typically introduce the term "economic development" or "the economics of community development"[1] in an effort to narrow the field somewhat, but still there is wide diversity. For example, Berry [3] and representatives of CSRS [5] indicate that provision of jobs or creation and maintenance of an employment base is the major objective of economic development. Spiegleman, Baum, and Talbert [12] suggest that "the essential goal of planning for economic development is to increase per capita income." In a somewhat different approach, Daberkow [6] used principal component analysis to weight 12 "selected" variables to form an "index of economic deveopment."

Without doubt, the criteria indicated above are important components of economic development. However (as will be shown in this paper), these are limited criteria; i.e., they represent only aspects of economic development

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[1]Castle [4] has made this distinction in a seminar paper relating the conceptual framework of natural resource economics to rural development.

and hence fall into the category of proximate criteria. The possible pitfalls of using proximate criteria have been delineated by McKean [10]. Suffice it here to point out that if economic development is a multidimensional concept and we as economists fail to recognize it as such, then our research results may be subject to serious question. The remainder of this paper is devoted to (1) identifying general components of economic development, (2) showing the subjective nature of these components, and (3) considering implications for the role of economists in developmental decision making.

We start with the assumption that economists as social scientists are concerned with increasing the economic welfare of individuals or groups of individuals. We contend that such an increase may be termed "development." Moreover, if the group is identified as a community, then an increase in aggregate welfare may be termed "community development." This, of course, merely shifts the burden from defining economic development to defining increases in economic welfare.

Before proceeding, one caveat should be extended. Henderson and Quandt [9, p. 201] point out that, "it is reasonable to postulate that the concept of social welfare transcends the more restricted notion of economic welfare." The concept that we wish to pursue is that of economic development. Hence, the goal of concern is economic welfare. This is consistent with Castle [4].

One may begin the process of conceptualizing economic welfare by postulating that it depends upon the quantities of all goods and services available for consumption and, to the extent that there may be scarcity, the distribution of those goods and services among the individual members of society. The phrase "goods and services" is used in a very general context.

It refers to both market and extramarket goods and includes discommodities as well as commodities.

If the effects of goods and services and distribution are separated into market and extramarket effects the relationship may be stated as

$$W = w(A_1, A_2, E_1, E_2) \tag{1}$$

where

W denotes aggregate economic welfare,

A_1 denotes effects of those goods and services with relevant prices or reasonable proxies thereof (market effects),

A_2 denotes effects of those goods and services without relevant prices or reasonable proxies thereof (extramarket effects),

E_1 denotes equity (distributional) effects of A_1, and

E_2 denotes equity (distributional) effects of A_2.

Obviously, equation (1) is intended as a pedagogical device rather than a mathematical function.

The problem in defining welfare as presented in equation (1) is that in this form the concept is not operational. Most economists agree that problems of interpersonal utility comparison and interdependency of individual utility functions preclude the use of a social welfare function as an operational criterion for judging the social desirability of alternative economic states. However, if such information were available; i.e., if we had the wisdom, techniques, and data needed to overcome these two problems, then the status quo could be compared with the aggregate welfare value resulting from the expected economic changes of a planned developmental program. If the welfare value change were positive, then it could be claimed

that welfare and, hence, development had been enhanced.

Although ability to determine levels of aggregate welfare would be desirable, it is not mandatory for most community development decisions. The need, most often, is an ability to compare welfare effects of implementation versus nonimplementation of a specified proposal. One need not be concerned with every aspect of economic welfare but only with those components which would differ from the status quo. Equation (1) provides a useful framework for such comparisons. A proposed project must be examined with respect to market, extramarket, and equity effects.

Market effects[2] (A_1) represent that component of economic welfare with which economists have historically been concerned. The value of market goods may be measured in dollars because of the ability of consumers to express themselves in the marketplace through the medium of a general good, money.[3] When measuring the incremental market effects attributable to a developmental program, both direct and indirect benefits and costs must be measured. In addition, uncompensated nonpecuniary externalities must be included. Although we recognize that an *a priori* measurement of these benefits and costs is at best a difficult proposition, it should be possible to derive a net figure which represents a net market component of a proposed program.

Because market prices (or reasonable proxies thereof) are not or cannot be determined for extramarket goods and services (A_2), such effects must be

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[2]Space limitations preclude a thorough examination of A_1, A_2, E_1 and E_2 effects. For a more detailed account, see [2].

[3]An excellent discussion of the deficiencies and advantages of using observed market prices is given by McKean [11].

considered as a separate issue. The analysis of extramarket effects is similar to that of market effects in that there may be direct changes in extramarket goods resulting from a developmental program and/or resulting from nonpecuniary externalities. It is, of course, obvious that since no common measure is available for most extramarket goods, they cannot be added or traded-off. Indeed, in some cases normative judgments might be required to decide whether a specific change is positive or negative. Therefore, the changes may only be described, and described individually. It should be further noted that there is no way of comparing market goods and extramarket goods using equivalent units. If an extramarket good can be compared in commensurate units with market goods, then it belongs in the market good category.

In equation (1) it was hypothesized that welfare depends not only upon the quantities of all goods but also upon the distribution of those goods. If a proposed development project alters the quantity of goods relative to the status quo, then there *must* also be distributive implications. Obviously, this pertains to the distribution of both market and extramarket goods. The distributional component has long served as an impasse in welfare economics. At the heart of this problem is the fact that so long as one person is made worse off, the inability to measure that loss and trade it off against some immeasurable gain by others precludes *proof* that welfare has either increased or decreased. Yet, it is normal for a developmental program which encompasses a large group of people to leave some of them with less market or extramarket goods. However, even in the extreme case in which the total quantity of goods and services is increased and no one has less than he had previously, it is still impossible, because of interdependent utility functions, to establish

an increase in welfare. For example, one person whose absolute quantity of goods and services is unaltered may view himself as being worse off because he has relatively fewer goods and services. Consequently, distributional effects, E_1 and E_2, can only be described and, in our view, must be treated as separate and distinct issues.

This brief examination of equation (1) components indicates that each must be analyzed independently. To unambiguously establish an increase in economic welfare, it must be shown that none of the component effects are negative while at least one is positive. This is difficult in the case of market goods because of measurement problems, more difficult in the case of extramarket goods because of aggregation problems (i.e., there is no agreed upon common denominator for aggregating dissimilar extramarket effects), and impossible in the case of distributional effects unless independent individual utility functions are assumed. These problems will continue to exist until a grand social welfare function is developed, complete with a set of explicit value judgments (a weighting scheme), which would permit the analyst to resolve the problem of incommensurability of the various components of social welfare. This roughly approximates the Bergson criterion, about which Baumol [1, p. 300] points out:

> Essentially, the Bergson criterion must be judged right, if not very helpful...(it) unfortunately does not come equipped with a kit and set of instructions for collecting the welfare judgments which it requires.

What, then, is the upshot of all this? We conclude that for practical purposes it is impossible to identify whether economic welfare of a community has increased as a consequence of a developmental program.[4] We doubt

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[4] It should go without saying that an inability to establish an increase in welfare does not mean welfare has decreased, nor does it mean that a particular project should not be undertaken.

that it will ever be possible for economists to consolidate components of economic development into an unambiguous unidimensional criterion. Attempts to identify when and where economic development has or has not occurred are mostly an exercise in futility, and perhaps worse, such efforts are likely to be deceptive and misleading for the clients of such research. To equate a word such as development--a word with all sorts of "goodness" implications--with events (e.g., increased per capita income or increased employment base) that may (in some instances) yield a decrease in community welfare is unfortunate.

While it is our contention that economists are (for the most part) incapable of rendering positive judgments concerning whether a proposed developmental project will or will not enhance economic welfare and, hence, development, the fact remains that decisions will be made. Many of the decisions regarding rural area development strategies are made at one or more levels (be it federal, state, or local) of the political process. If this decision making process is to function, obviously some criteria, implicit or explicit, for judging developmental impact will be adopted in order that decisions may be reached. That is, decision makers collectively or individually will adopt means for weighting or comparing the components suggested in equation (1).

Fox [8] has suggested criteria for judging and methods for improving the decision making process. He has noted:

> Studies lead to the conclusion that there are not universally acceptable value criteria which can be applied to determine whether a given program produces an optimum social product. This leads to a recognition that a program must be judged by the process through which it is decided upon rather than by some measure of the consequences of the program itself [8, p. 30].

Fox's criterion is not as alien to economists as it might first appear; he notes elsewhere that an important aspect of effective social decision making is the identification and evaluation of alternative courses of action [7, p. 31]. The developmental economist's burden is to provide the kind of information indicated in equation (1); i.e., information on (1) market effects, (2) the effect on extramarket goods insofar as they may be described, and (3) equity or distributive effects. The burden of weighing these elements and making final decisions falls upon those who are responsible to the people affected by the implementation or nonimplementation of a developmental program.

The notion that economists might or should undertake a larger role in the developmental process is moot because the hope for an agreed upon unidimensional gauge of economic development is a false hope. Indeed, perhaps the concept of economic development is itself a mirage. Be that as it may, there remains plenty for community development economists to do in the *economics of development* arena.

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