





३५



R/ =

N 7

7/50







THE ECONOMICS OF  
FULL EMPLOYMENT  
IN AGRICULTURAL  
COUNTRIES



*By the same author*

“CEYLON BEVERIDGE AND  
BRETTON WOODS”

“The notion that successful development from one economic situation.....to another might be a more crucial test of the contribution made by an economic system to human welfare than the attainment of perfect equilibrium in any given situation seldom commanded attention.”



THE ECONOMICS  
OF  
FULL EMPLOYMENT  
IN AGRICULTURAL  
COUNTRIES

*With Special Reference to  
India and Ceylon*

BY

C. SURIYAKUMARAN

B. A. (CEYLON) B. SC. ECON. (LONDON)



*Publishers*

K. V. G. DE SILVA & CO.  
COLOMBO AND KANDY



331  
SUR

FIRST PUBLISHED IN 1957



### ACKNOWLEDGEMENTS

*With thanks to the several typists for their ready co-operation at various stages of this book; to the friends (chiefly Mr. M. Balendra of Bank of Ceylon) who helped in comparing and proof checking; to the Printers for their willing co-operation; to R. S. R. Candappa for almost all the ideas on and the entire design of the cover and text presentation; and to the Publishers for making every aspect of this Book, from appearance and printing to final distribution, so personal a concern.*



PRINTED AT  
THE ASSOCIATED NEWSPAPERS OF CEYLON, LIMITED,  
LAKE HOUSE, COLOMBO.



# CONTENTS

			Page	
PREFACE AND NOTE	...	...	...	XI
PART I				
CHAPTER 1	Introductory	...	...	3
	Nature of the Problem			
CHAPTER 2	The term "Agricultural Countries"	...	...	6
	Content and Meaning			
	Agricultural country — Underdeveloped economy — Balanced economy — Wages goods industries — Further elucidation.			
CHAPTER 3	The Economics of Agricultural Countries	...	...	11
	Treatment — Supply — Demand — Location — Size — Middlemen — Income earning ability — Fluctuations — The State — Agricultural Countries — Solution.			
CHAPTER 4	The Theory of Full Employment	...	...	31
	Antecedents — "Accepted" Theory — Limitations — Integration — Diversification — Post-Keynesian analyses — Economic dynamics — Investment Boards.			
PART II				
CHAPTER 5	The term "Full Employment"	...	...	51
	Employment for all — Standard of living for all.			
CHAPTER 6	The Case for Development	...	...	58
	Poverty of means — Certain factual data — Implications for the industrial countries — For the agricultural country.			
CHAPTER 7	The Field for Industrialisation	...	...	80
	Type of investment — Export industries — Import replacing industries — Home industries — The term 'industrialisation' — History — Principle of Development.			
CHAPTER 8	The Machinery for Full Employment	...	...	89
	The problem — Fallacies — Complementarity of industries — Other objectives — Financial methods.			



## PART III

	Page
CHAPTER 9 The Structural set-up in two Agricultural Countries—India and Ceylon	103
<p>Countries selected — Purpose of this chapter — Under employment, definition, measurement, types — Productivity in agriculture — Secondary and tertiary sectors — Foreign Trade. Ceylon — Rural background — The plantations — Secondary and tertiary sectors — Foreign Trade — Capacity of the existing economy — Production possibilities.</p>	
CHAPTER 10 Policy for Full Employment	
I—The structural Framework ...	151
<p>Rectifying the impediments — Population — Savings, hidden savings — Demand for income — Industry and agriculture — Planning — Output, agriculture vis-a-vis industry, the scissors — Size — Risk — Isolationism — Basic industries, wages goods, diversification — Economic re-organisation, agricultural and industrial — Location — The unit for industry and cottage industries — Transport and marketing — Training — Finance and credit — National Development Corporation — The plantation industries — Export industries — Research — Domestic industries — Summary.</p>	
CHAPTER 11 Policy for Full Employment	
II—High Cost Industry, Fiscal Policy and Social Security ...	197
<p>Question of high costs — Validity of protection — Measures for protection — Industrial Products Bill (Ceylon) — Fiscal Policy and social security — Certain aspects of subsidy.</p>	
CHAPTER 12 Policy for Full Employment	
III—Planning	216
<p>Its fundamental nature — Its gradations — Consumer's choice — Modus Operandi — Theoretical model — The Colombo Plan — Some implications of planning — The Budget — Exchange policy, appreciation and devaluation — Inducements to investment — Wages — Prices — Selling — Dynamic Economic — Some estimates of costs.</p>	



## PART IV

	Page
CHAPTER 13 Internal Full Employment and World Economy ... ..	263
<p style="margin-left: 40px;">External influences — I.M.F., World Bank  — International economic equilibrium —  Havana Charter — Regionalism — Multi-  lateral regionalism — South-East Asian  Currency Area — Summary.</p>	
CHAPTER 14 Re-instatement of General Theory ...	280
<p style="margin-left: 40px;">Employment for all — Residual unemploy-  ment — Frictional unemployment — 'Epidem-  ic' unemployment — Rentier functions —  Dynamic forces — International currency —  World Trade Organisation.</p>	
CHAPTER 15 Summary and Epilogue ...	287
<p style="margin-left: 40px;">Summary — Future and the competence of  economic theory.</p>	
Bibliography ... ..	300





## PREFACE

SOME years back when this Book was being contemplated, the domination of Keynesian theory was still strong. It was supposed that the 'accepted' devices for full employment were equally valid in almost all contexts. It was not sufficiently realised that the relevant theory had been largely inferred from and was mainly applicable to countries with diversified and well-integrated structures of production. It was, in other words, felt that these devices would effect large-scale transformation of the structure and trends in production of under-developed countries; whereas, in truth, this large-scale transformation had first to be effected by other means before full employment theory could be considered applicable. The latter is now more or less commonly accepted fact.

So also is the view point in favour of incorporating Industry in general development. It is a point of view that may have required much proving a couple of decades back.

An aspect of this subject, however, remained a matter of controversy for a longer time. It was the effectiveness or otherwise of the normal machinery of 'private commitments' in working the change. There was a theoretical error in assuming that the history of development of the advanced countries could provide the answers to the problems of executing the change in agricultural countries. It was not fully granted that the context of depressed countries developing in the midst of far advanced ones is poles apart from the nineteenth century context of dynamic national States forging ahead amidst positively stagnant economies. But the role of the State as a participant in economic development is more clearly understood now, although on the degree of participation there is still much disagreement.

Attempts to show the irrelevance of full employment theory have appeared sporadically, as foot notes and passing observations in articles or books. Some articles and books on the subject of under-developed areas have, by the emphasis placed on structural change, shown the secondary importance of accepted full employment theory for these countries. Similar discussion has been evident in regard to industrialisation in backward countries.



In regard to the necessity for the State to assume a more intimate role in development than formerly there has been more direct literature.

The purpose in Parts I and II of this Book has been to bring together, critically, the relevant arguments that may have appeared at various times and contexts ; to supplement, where other literature has not already covered the points ; and, thus, to set down the theoretical foundations on which the current general acceptance of the three points, referred to, are based.

In Parts III and IV the appropriate economic policies, internal and international, dictated by the foregoing are considered with special reference to India and Ceylon (more particularly the latter). The economics here is largely one of change and how to effect that change. A Study in the Economics of Transition could well be a sub-title to the Book.

No hard and fast, universal or detailed applicability is necessarily claimed for the analysis and conclusions in the Study. An effort has been made to bear in mind the words of the Introduction to the Cambridge Economic Handbooks by Keynes that "The Theory of Economics . . . . . is a method rather than a doctrine, an apparatus of the mind, a technique of thinking, which helps its possessor to draw correct conclusions." The object of the analysis has been, again in the words of Keynes (in the General Theory) "not to provide a machine, or method of blind manipulation, which will furnish an infallible answer, but to provide ourselves with an organised and orderly method of thinking out particular problems ; and, after we have reached a provisional conclusion by isolating the complicating factors one by one, we then have to go back on ourselves and allow, as well as we can, for the probable interactions of the factors amongst themselves. That is the nature of economic thinking."

The writer wishes to acknowledge with gratitude the personal discussions he was fortunate to have on certain branches of the subject of the Book with Mr. M. H. Dobb, Trinity College, Cambridge, with Dr. Karin Koch, Director of Planning, Stockholm and with officials of the Ministry of Commerce (and Planning) Oslo.



The writer is also grateful for certain suggestions for further reading etc. by Dr. B. B. Das Gupta of the Research Department of the Central Bank of Ceylon and by others here and abroad.

My grateful thanks also to certain leading persons at one time or another connected with economic development in this country, and to three Economists here, in India and in England for so kindly permitting me to thrust this work on them and test their reactions, before launching it on the public.

---

### Note

The World Bank Mission's Report on Ceylon came out in September 1952 and could not be considered in the body of the Book. It happens, however, that the various theoretical subjects raised by it have been referred to and discussed. The Institutions required for development, Selection of industries, Priorities, Exports, Research and Subsidies, to mention some instances, have been discussed. Therefore, although no direct reference to the Report is made, this may be presumed wherever such subjects as those referred to here are taken up in the ensuing pages.

The writing of this study was finished in 1952. The surprising thing however, on looking back, is that, except for the fact that some points could be illustrated by more recent data, the defects that need pointing out and the policies that need advocating still need to be pointed out and advocated. There are, of course, many aspects—irrelevance of General Theory, the comparative cost inferences, the South East Asian Currency Area, certain aspects of planning, and some others—which would have been 'newer' then. But that is another matter.

Colombo, Ceylon. 1956.







**PART I**







## INTRODUCTORY

A STUDY of the economics of full employment in agricultural countries would pre-suppose that the nature of the unemployment problem in such areas, or the problems of securing and maintaining full employment, or both, are different from those in the more advanced economies. That pre-supposition is not misplaced. In the industrial countries of the West, unemployment has been largely characterised as an accompaniment of depression in the cycle between prosperity and slump. The static condition of massive under-employment, as exists in and keeps stagnant several agricultural countries, has hardly been adequately recognised or discussed in most analyses of the unemployment problem. When Theory talks of 'chronic' depression the reference is merely to the unduly (and unexpectedly) prolonged lag in investment activity viewed as a trend over a couple of decades or so. The term structural depression is not of much interest to agricultural countries since their structure is for the most part 'one-storied' and composed of very few and simple types of economic activity. The differentiation between partial and general depression is also of little interest to agricultural countries depending for national income and life on a very few large sources of production. A depression is a general depression. If it does not affect any indigenous (as opposed to export) agriculture or sections of the population, it is only because these parts, even before the depression, were fairly at rock-bottom level. To describe the cyclical inflections that come on these countries as a result of the industrial-agricultural-dichotomy in an economic One World, these subtler divisions into types of depressions would be somewhat superfluous. They may enable the development of finer thought in economic policy and suit the purposes of industrial countries. They would give a totally wrong emphasis, in the case of backward agricultural countries. The mere phrase 'Cyclical Depression' would suffice.

The important point is that besides severe unemployment, there has been chronic and depressing under-employment in most agricultural countries. We might with profit use the phrase Chronic Depression to refer to this malady in the typical agri-



cultural country. It can mean under-employment almost amounting to endemic unemployment and manifesting itself, in depression, only as famine and decimation.<sup>1</sup> The causes for this would lie in an absence of co-ordination or full utilization, or a scarcity, of some or several of the factors of production. This should result in a vicious circle and a standard of living lower than physiological subsistence level. An examination of the reasons for this level is one of the purposes of this thesis.

It will be fairly clear, therefore, that the nature of the unemployment problem itself is, for various reasons, so different in degree or quality, that it would alone be sufficient ground for a separate study of the subject. There is however a further factor, in a sense a corollary to this, which would make a separate treatment clearly imperative. The "armoury" of 'devices' provided by Full Employment Theory and applicable to the well integrated diversified economy with a highly advanced credit structure and a capital market, are of little relevance in the simpler and relatively backward structures of the agricultural economies. Even assuming that factors wherever used are being fully employed and the problem of unemployment is absent, still an attempt to apply the general principles of Full Employment Theory will be found insufficient and sometimes dangerous. That the problem is made only far worse by the further existence of under-employment is, of course, self-evident.

In short, the theory of Full Employment has been inferred from and is applicable in practice mainly to 'advanced' countries with diversified and well-integrated structures of production. The differences between the advanced and 'backward' economies being thus, in a sense, fundamental,<sup>1</sup> it is only to be expected that in certain vital and hitherto neglected aspects of economic policy the conclusions derived may be contradictory to the hitherto freely accepted notions for the prevention of depressions and the securing of a high and stable level of employment. Among these neglected aspects of economic policy are, international trade, its nature,

---

1. c.f. W. A. Lewis, 'The Principles of Economic Planning', page 122, (Appendix on Planning in Backward Countries) — "In advanced countries the national income increases steadily from decade to decade even if the government does not 'interfere' in economic life. But in many backward countries there is either stagnation or retrogression...."



trend and quality, tariff policy, outlook on industries and their individual profitability, the various types of approach to giving a balance to the economic structure, the degree and type of Planning and planned interference in economic activity.

We shall therefore, in the subsequent chapters, amplify and examine the various considerations arising from the foregoing observations. We shall also work out in outline an employment policy with particular reference to India and Ceylon.



## CHAPTER TWO

# The term "Agricultural Countries"

### CONTENT AND MEANING

THE term 'agricultural country' is quite familiar and its use is, generally speaking, well understood. It is not considered very different from the phrase 'under-developed economy' that is so often used today. It would appear that the former label had no need to be replaced during the earlier decades, when international trade on a two-way traffic, of agricultural goods from one set of countries and industrial goods from the other, prospered. The changes that followed the violent slumps of the inter-war period, with their focus on insulation against shocks and on full employment, called for diversification and, especially, general development. Apparently the word under-developed was a more apt description of what was formerly known as an agricultural country.

For several purposes it is a matter of indifference which term we use. But from the angle of full employment theory—and that is our angle—the term agricultural country seems more useful. It will be seen, in the later pages of this thesis, that the difficulties in the way of achieving and maintaining 'full employment' are not overcome by development agriculturally alone, although certain other benefits will accrue therefrom. Logically then, it is not the under-development in existing agriculture alone that is responsible, but the lack of a 'balance' in the economy. Besides, a country may be 'under-developed' (through lack of coal and iron industries) but 'balanced' if it is structurally suited to the operation of full employment devices. It is also not often remembered that so-called industrial countries are not a forest of industrial centres and towns but have considerable sections of the economy under agriculture, involving, in several instances, enormous quantities of capital investment, output and even manpower. Colin Clark,<sup>1</sup> writing in 1939, noted, for instance, that France had a higher income from agriculture than from industry "until recently".

1. Conditions of Economic progress, pp. 12 & 5. Chs. 10 & 4 (All references are to the 1939 edition).



He even termed the country agricultural. In our sense of course it would not be really agricultural.

The economics of full employment operates best in a 'balanced' economy, worst in a purely agricultural economy, and with fair success (given satisfactory conditions of international trade) in a purely industrial economy. Purely agricultural countries in the sense are very rare. A definition on these lines may apply only with varying degrees of imperfection. To help us get to the core of our problems, however, such a definition is both necessary and helpful. It may be best then if instead of the term 'agricultural' we used the term 'balanced' (again with varying degrees of imperfection) to refer to those countries which may normally be designated agricultural, but which have a vigorous industrial set-up as well ; and to mean by agricultural only such an economy as has very little industry.

In this sense well-diversified 'agricultural' countries like Denmark, Canada and so on may be termed 'balanced', while the more imperfect economy of India and especially of Ceylon will be termed agricultural. The idea in the term 'balanced' is that, in it, the features of modern full employment theory and policy find the essential prerequisites for successful operation and achievement of the objectives. It is not the degrees of development but the basic economic foundations that we are thinking of. This sense, one feels, gives a proper isolation of the irrelevant from the relevant features in the economics of full employment. (In passing, it may be admitted that on this footing most of the so-called industrial economies are more properly termed balanced economies and that the term industrial stands, with varying degrees of relevance, for the extreme cases alone).

Assuming lack of 'balance' to be the basic differentiating factor in the countries we have in mind, we could provide an efficient definition by stating that they possess an undiversified structure in the sense of a lack of certain wage-goods industries. It is evident that a more comprehensive identification is achieved by calling these countries agricultural rather than under-developed. It may be asked, however, why it is insufficient to describe an agricultural country as one which is overwhelmingly agricultural. Such a definition does not seem to focus attention correctly on



the points that, for full employment, make an agricultural country different from a 'non-agricultural' country. As we shall see, what marks off the success of devices for full employment in the latter from failure in the former, is not the absence of any industry but the absence of wage-goods industries chiefly. The small proportion of agriculture in an economy, as against mining for instance, does not make that country non-agricultural; an overwhelming proportion of agriculture vis-a-vis the rest of the economy does not make it agricultural, if at the same time there is an appropriate range and number of wage-goods industries.

Having emphasised the central deficiency of the agricultural country, we may note that the term under-developed serves one very useful purpose. It is to emphasise that most agricultural countries have even in existing lines of production low incomes—a result largely of low capital investment and poor organisation. We shall see this to be a serious obstacle to the credit and fiscal devices for full employment in the countries we shall discuss. As such while, technically, the above definition may be proper, we may for our purposes define a typical agricultural country by adding the latter concept of low-income to the previous basic feature. Agricultural countries, then, are countries possessing an undiversified structure, in the sense of a lack of certain wage-goods industries, especially in a general state of under-development of the economy as a whole—under-development being understood in terms of the existing technical efficiency and economic organisation.

Certain observations may be briefly made by way of further elucidation. First, our definition covers the case of economies based on mineral production. Second, neither income levels, nor proportions of agricultural to total capital, total employment or total output, are any complete test. Third, lack of diversification often manifests itself in an acute form when an economy is built round the export trade on raw materials and/or food. A depression in such a context is hardly structural or partial, for the entire economy is soon dragged down. This goes for high income countries as well, except for the point that the high normal incomes may be used for a Social Insurance Scheme. Finally, two corollary points follow, which we shall only mention for the moment. A pursuit of the accepted full employment policies results in signi-



ficant leakages of the multiplier abroad ; secondly, the internal economy is not structurally capable of responding to a reinforcement of purchasing-power. In the state of general under-employment that exists in several countries, the unfortunate consequences follow even more rigorously.

The under-developed economy was recently defined by Hicks as one which suffered from chronic unemployment which was associated not with unsold surpluses (as in the case of a mature economy in depression) but with shortages and scarcities.<sup>1</sup>

The intention in the phrase 'chronic unemployment' presumably includes under-employment. It should be mentioned, however, that surpluses in agricultural countries are hardly rare in the great exports of food and raw materials—in the same way as during depressions there are surpluses in industrial economies. It is true of course that 'chronic unemployment' connotes low incomes and chronic limitation of the volume of goods available for human needs. But it is doubtful whether the definition is guide enough to identify the countries we are after. Besides there are 'under-developed' countries whose malady is not chronic unemployment but fluctuations in employment levels, to which countries too the prescriptions of Keynesian theory are largely inapplicable. It really seems that the operative features of the countries we have in mind lie (a) in the lack of wage-goods and (b) in the nature of the agricultural organisation.

To the extent that these deficiencies are less serious in real fact, the countries become less typically agricultural and so more amenable to accepted full employment methods. The under-employment is not the first cause. Poor technique and weak organisation seem fundamental causes. The experience of the less depressed agricultural countries would show, however, that diversification of the economy through introduction of wage-goods industries is the final distinguishing feature.

The following excerpt from the Report of the League of Nations Delegation on Economic Depressions, throws interesting light on our discussion. "The problem of depressions in primary producing

---

1. At Delhi University, Feb. 1950, vide *Eastern Economist*, Feb. 10th, Page 211.



countries is in many ways different, both in its origins and its manifestations, from that in industrial countries . . . There are several distinct groups of non-industrial countries which are somewhat differently affected by cyclical movements although they naturally shade into one another ; so that a clear-cut classification is not possible." Three groups are distinguished in the classification. The first "consists of agricultural countries with a low income per head, such as India and China and, to a lesser extent, parts of Eastern Europe in which capital and in some cases land, are relatively scarce compared with labour. This relative scarcity of capital and land keeps down productivity, so that the majority of producers live at or near subsistence level." Of course this academic extraction obliterates the fact that, for instance, in Ceylon this problem co-exists with the problem of unstable agricultural exports responsible for as much as half the national income. Still the distinction is useful. "The second group of primary producing countries consists of countries such as Australia, New Zealand or the Argentine, in which land and capital per head of population are abundant and the standard of living relatively high. These countries are largely dependent on outside markets, and are particularly sensitive to the effects of depressions in industrial countries on the demand for their exports as well as on the flow of capital imports". The effect on Capital imports is coupled with the obligation to meet unchanging money charges in foreign currencies on account of debt services. Their incomes fluctuate "mainly as a result of price movements and less through variations in the volume of output . . . The third group of countries consists of those, whether heavily populated or not, whose national income is largely dependent upon the export of minerals. In this group would fall for instance, Bolivia, Burma, Columbia, Rhodesia, South Africa and Venezuela." In these countries the incomes derived are "likely to be influenced by changes both in the quantity and in the price of their exports". "This phenomenon" adds the report "presents itself to some extent also in the case of certain agricultural countries exporting agricultural raw materials or semi-luxury goods" for instance, rubber or tropical fruits.



## CHAPTER THREE

# The Economics of Agricultural Countries

(i)

**T**HE treatment in this chapter falls broadly into two parts. In the first, there is an attempt to bring out some significant points in regard to the economics of agriculture generally.

In the second, a brief bird's-eye view of the agricultural economy as it operates is given. It is not the intention to enter into a detailed study of the economics of agriculture as such. The investigation in the thesis is into the relevance or irrelevance of 'Keynesian' prescriptions for full employment and the consequent alternative measures called for by it. The observations on the economics of agriculture are therefore related to the purposes of our next chapter on the theory of Full Employment, and to the problems raised by it. It is not their objective primarily to be a theoretical version of the economic backgrounds we describe in Chapter 9, of India and Ceylon. There are several characteristics in agriculture that would be universally valid and naturally enough such principles fit the cases of India and Ceylon. However, there are several characteristics in addition in India and Ceylon, like the nature of the capital investment and of land organisation, which would not be universally valid or at least universally crucial. The present chapter seeks to select certain characteristics that we may take to be universally crucial, and to establish in conjunction with the second part of the chapter the ground for certain important contentions in the next chapter. The points raised in the present chapter will also afford a useful background for the special agricultural difficulties cited as existing in India and Ceylon in Chapter 9.

The extensive use of land as a factor of production,<sup>1</sup> the peculiar dependence of agriculture on land, and the dominating tendency, of diminishing returns, are as familiar as they are relevant to the problems of the agricultural countries.

---

1. Note also that land cost is a preponderant part of factor cost in a farm-unit. This is corroborated not only by experience of 'Western' agriculture. The average rural family in Ceylon had in 1950 a stock of property worth Rs. 2,171. Land took up Rs. 1,063 of this total, with Rs. 86 for livestock, Rs. 381 for household and other goods and Rs. 641 for buildings. Household and other goods not being related directly to agriculture, the omission of this item shows the predominance of land as a factor even more. c.f. Sessional Paper (Ceylon) XI of 51, p. 13.



## (ii)

The ability or otherwise of *Supply* to meet changing situations is the first striking feature to be assessed.<sup>1</sup> There is, for instance, the inter-relationship between different products. In common with industry, there is a composite demand by all products for the various factors of production. So that under certain conditions output of one can only be at the expense of the others. In some cases, like milk, and meat, the competition is closer and more obvious. On the other side, under mixed farming, several items are joint products or by-products. Increase in output of one facilitates output in the others. But costs attributable to one cannot be separated as in industry ; nor can production of one be increased or reduced to meet the appropriate change in demand without affecting, through the other, the assurance of maximum net profit. It is a difficulty largely avoided in the case of industrial joint or by-products. In terms of time, the dependence on land and on gestation periods militates against elasticity in supply. The long 'chain' between producer and ultimate consumer is a factor to which we shall refer in more detail very soon. Among the other factors may be mentioned the smallness of the units vis-a-vis industry, the relative lack of division of labour and of intensive specialisation, and the dependence on the weather and natural factors connected with plant and animal. Finally, one may also mention the social, political and sentimental factors influencing or conceded to the peasantry. In the result, supply adjusts itself only slowly to price changes.

In the theoretical long period, a rise in price vis-a-vis industry, would by increased profitability, divert factors and increase output till relative equilibrium was again established. But an increase in output in agriculture is likely to involve decreasing returns especially in densely populated countries. It raises costs and thus prices, while an increase in industrial output has generally the opposite tendency. The point at which diminishing returns will appear in industry is postponed easier than in agriculture. In any case, the long period supply curve is purely theoretical, for the period is

---

1. R. Cohen's "The Economics of Agriculture" has been considerably utilised for the argument in the first half of this chapter. The quotations unless otherwise mentioned are from this source.



too long for several factors like prices and so forth to remain stable. The short period curve differs from the long. What is more, the difference between agriculture and industry is more prominent in the short period. In the very short period, it is largely a mere question of relative helplessness, if the purpose is to increase supply ; and in the opposite case, of letting the stuff go waste rather than incur the expense of bringing it to market. (In some cases as in cattle which are not so perishable, a reduction can be effected by lowering the rate of slaughter.) The more relevant short period is that where time is given to plant or breed and thus increase supply, or vice versa. It really merges into or is, the middle length, and ultimately merges into the long period. In industry, too, there is a lag between decision to expand output and the increased supply. The point however is that in agriculture the lag is generally longer—in some products it may be six months, in others anything up to five or ten years. Even thus a farmer can often only intend to produce more—natural factors beyond control can affect output considerably, and have done so. There is also the point that, in certain branches at least, less attention is paid to prices than in industry.

Given the possibility of altering output in the long period, to what extent is it profitable to do so? There is, of course, the fickleness of conditions of demand. The larger the lag, the more likely it is that, for any one or other of a host of reasons, demand for a product having once increased (or decreased) may later as easily fall (or rise) by absolute change, or by relative change through demand for substitutes and synthetics, and for reasons monetary or real. Apart from this, there is, on the supply side, the peculiar relation of prime to overhead costs in agriculture. Prime costs are considerably smaller and exercise certain influences on output peculiar to agriculture alone. Prime costs are the only amounts which would affect output. One may say in a general way that, except in the long period, prime costs in agriculture are almost always lower than overheads. There is also the point that, unlike



machines in industry, if land is not worked, it deteriorates more and involves later expense of clearing and so on. It may be assumed that in any occupation, the entrepreneur "will stay in business so long as total returns exceed prime costs by at least as much as he can earn elsewhere by his own labour and with the aid of the equipment which he owns or must pay for whatever he produces". Whether a price decline affects agriculture generally or both agriculture and industry, given the above conditions, it will still not be profitable for the farmer to cease working. "The shorter the period allowed the fewer items will be included in prime costs and therefore the less likely is it that the farmer will give up his farm". As for a price rise, difficulty of easy credit and sub-marginal land as the only available factor, will all militate against quick change in output. There is also the factor that an agricultural family may produce more, if prices fall, to maintain incomes; on the other hand, working already long hours they may not be able to work longer hours still. These are contradictory tendencies and which will show depends on the individual instances and reactions. If prices rise, the family unit may work and produce less. Incidentally, wages are much less sticky in agriculture and contribute to make any decline in output, as prices fall, certainly less. A convincing proof is the fall, in world output during 1929-32. On League of Nations statistics, industrial production fell by 37% and non-agricultural primary by 31%, while agricultural production fell only by 1%.

The foregoing explanation presumes that the response of agricultural output during cycles is peculiar to it. Indexes of production under Agricultural Output, Manufacturing, Durable Manufacturing, Non-Durable Manufacturing, Iron and Steel, Machinery, Mining, are usually considered in illustration of the point. But in a recent well-reasoned discussion<sup>1</sup> the following table was produced to show "that there were other important segments . . . which produced almost as much in 1932 and 1933 as in 1929".

---

1. D. Gale Johnson, The Nature of the Supply Function for Agricultural Products, American Economic Review, September 1950 pp. 539 et seq.



**1933 Output as a percentage of 1929 Output**

Meat packing	...	95
Shortening	...	98
Canned milk	...	98
Cheese	...	95
Butter	...	110
Cotton goods	...	87
Woollen and worsted goods	...	87
Knit goods	...	100
Shoes, leather	...	94
Beet-sugar	...	151
Canned fruits and vegetables	...	88
Clothing, women's	...	91
Soap	...	98
Petroleum refining	...	86

It was also noted that for several industries in the list, the cost of agricultural raw material was less than a fifth of total manufacturing cost. Therefore, the steady output in these industries could not be explained away by the steady output in agriculture. Of the explanations hitherto offered, that of high fixed costs has been the most accepted. The author, referred to, rejects this. We may note, in sympathy, that in plantations and similar areas where hired labour (or some other factor like rents) is more important, the argument of high fixed costs loses much of its force.

The other explanations usually offered are also listed (a) That farmers try to offset lower prices by increased output, (b) that subsistence production is important in agriculture, (c) that technological factors inhibit response to price changes, and (d) that agriculture has a more competitive structure than the rest of the economy. Argument (a) is granted a certain validity, but not considered a sufficient explanation; (b) is rejected with accurate data drawn for U.S. production (In Ceylon, the plantation output is almost entirely not for subsistence); (c) is considered valid for short cycles but not for a long cycle as in 1929-33; (d) is contradicted by the figures for canned milk, meat packing, soap and beet-sugar which are described as non-competitive. In addition several competitive industries like mining, lumber and lumber



products showed 'much smaller outputs in 1933' as against 1929. Degree of competition in the factor markets rather than in the product market is considered the more important.

The required explanation is provided, in the opinion of the writer referred to, by the usual economic analysis of profit maximisation, and the special characteristics of agriculture are explained by the "characteristics of the supply functions of factors to agricultural firms." In 'a major prolonged' slump, "farm prices, farm wage rates, and land rents would fall in proportion," to the fall in activity, and "employment of land, labour and machinery would not change appreciably." Current expenditure on depreciation and maintenance can be postponed for as long as four years.<sup>1</sup> The conditions of elasticity of land, labour and capital supply combine with the price behaviour of the other input items to maintain output. For example, 'supply price of factors used in producing livestock fell proportionately as much as the prices of livestock, and . . . livestock output was maintained.'

In passing mention may also be made of shifts consequent on price change of individual agricultural products. In the long run, the position is not peculiar to or different from industry (save of course the fact of increasing costs in agriculture). In the short run, the responses are different and born chiefly of the fact of several of them being joint products representing a composite demand for the factors. On the other hand, that a large amount of the capital equipment and much of the skill is more adaptable between product and product, makes for a response to price change. The overall effect, however, seems to be against any easy adjustment of supply.

(iii)

On the side of *Demand*, the peculiarities are equally distinct. With world agriculture overwhelmingly concerned with food, it may be said, generally, that additions to world purchasing power will be disbursed more on industry than on agriculture. The following list,<sup>2</sup> showing world output of the twenty most important agricultural products in 1927-30 in order of importance at U.K. prices, establishes the point that food is the dominant factor in agricultural activity :

- 
1. c.f. page 551 of the same Article for the data substantiating the statements.
  2. Cohen page 8.



- |                           |                     |
|---------------------------|---------------------|
| 1. Milk and milk products | 2. Eggs             |
| 3. Wheat                  | 4. Rice             |
| 5. Pig meat               | 6. Beef and veal    |
| 7. Maize                  | 8. Potatoes         |
| 9. Cotton                 | 10. Oats            |
| 11. Barley                | 12. Sugar           |
| 13. Rye                   | 14. Tobacco         |
| 15. Wool                  | 16. Mutton and lamb |
| 17. Wine                  | 18. Coffee          |
| 19. Silk                  | 20. Soya beans      |

Elasticity of demand being low, a phenomenal increase in agricultural production may leave unconsumed surpluses irrespective of a lowering of prices ; a rise in prices would not reduce demand either.

( iv )

The general capacity of agriculture to meet economic demands is also partly dependent on the question of *Location* of its types of produce. Land is not valued purely for fertility. In deciding the location of agriculture, the cheapness of some raw materials and labour costs in the country may vie with reduced costs of transport and manufactures, if the town is in proximity to the land. In this the preference of agriculture would be to exist as close to the market as possible. Yet the deciding factor is, ultimately, not the voluntary preferences of agriculture itself, but rather the forced ousting of agriculture by industries from positions in and around the markets. The reason, as has been observed, lies in their different intensities of production per acre of land. "Diminishing return from land will, therefore, not become important in industry until a very much greater weight of product is manufactured on the land than could possibly be grown on it in agriculture. To a considerable extent the large number of people employed per acre in industry means that industries themselves create towns, and hence markets both for industrial and agricultural products. In addition towns, in themselves, tend to attract industries. The attraction depends—generally speaking—on the weight of product produced per acre." Suppose one hundred units of a commodity



are manufactured per acre, and only one unit of an agricultural commodity grown. If transport costs are proportional to weight, the savings obtained by manufacturing the former close to the market will be hundred times as great as the savings from growing the agricultural commodity there. For this reason industry will be able to offer a higher price than agriculture for land which, because of its position in relation to the market, is most desirable for both occupations. It is the relative pull of the market, not its absolute pull, which is the deciding factor ; so that agriculture will tend to be pushed outwards from the market by industry. We may also note that the area nearest to the market will be the most productive in terms of value, and will, assuming uniform fertility, be the most intensively farmed.

As important as the location vis-a-vis industry is the 'locational' distribution of the different varieties of crops and of other agricultural produce over the agricultural area itself. Again the attractiveness of the market is of great importance, and is determined mainly by the cost of transportation. This cost is dependent on weight, bulk, perishability, fragility, and so forth. This would conform to the Von-Thunen zones presumed to lie between concentric circles, with the market at the centre. Of course, this regularity is markedly absent in practice for various reasons. Transport costs are cheaper along the main arteries like railways, roads and canals, and cheaper by water than by land. Besides, the market is not one place but several places in an Area or a country ; in fact every village and house is a market. Where the problem of transport enters only after any processing stage, for example milk for cheese and butter, or beet for sugar, the farms tend to cluster round a factory irrespective of somewhat better agricultural conditions further away. There are other reasons affecting location and localisation. The influence of natural conditions favouring a product is often a dominant factor. The benefit of mixed farming leads to the stultifying of the zonal pattern. Also, in populated areas, pressure on land prevents anything like the optimal combination of factors. Sometimes, even with no pressure of population, capital machinery cannot be combined as desired—for example in the hill country. In these circumstances, the only manner of securing an optimum in economic activity is, invariably, by mixed farming and by cottage industries. In the international plane,



not only natural conditions of area, soil, etc., but also relative labour costs influence and determine to a large extent, both the existence of certain countries as predominantly agricultural, and particular types of produce. Of course, if agriculture is a function of low labour costs, and low labour costs are a function of agriculture (natural resources and developed skill being the two underlying factors) then it is a vicious circle. It is part of the problems about which this Thesis is concerned.

To quote from Cohen, "Agricultural production will have to adapt itself to these changes. It will not, of course, do so instantaneously, so that production at any moment will be partially adapted to conditions which have disappeared. Adjustment may be hindered partly because the farmers are slow to realise the changes which have come about, and the legal relationships between landlord and tenant are slow to alter. Partly, however, it will not pay the farmers to readjust their outputs until their buildings and machinery, designed for one sort of production, need replacement. Thus the location of agriculture at any one time depends partly upon the conditions prevailing at the moment, and partly upon those which prevailed in the past."

( v )

A characteristic of agriculture that could be crucial to development is the *Size* of the agricultural unit. Size may be measured on the number of workers in a unit and the value of the gross output per that unit. It is not surprising that by both standards, the average agricultural unit is, generally, much smaller than the industrial. Several advantages exist to large scale undertakings in agriculture. Marketing economies (by reducing costs or increasing bargaining power) and the ability to sort into grades, for example tea, (by effecting a higher average price for the whole output) are important factors. Perishability is an adverse point, but not a result of large scale dealing as such. If co-operation is adopted, the large scale advantages accrue (by virtue of elimination of middlemen as well as other factors) to the medium and small size business as well. There are, also, the technical advantages of large scale units. They accrue through items such as farm buildings, the ability to use specialised and expensive machinery, and the scope for economies of specialised labour.



The scope, however, is not so much as in industry. Machinery cannot be used continuously and the advantages of specialised labour are relatively small and not as easy in mixed farming as in crops like tea. Besides, managerial difficulties constitute a serious limitation on the expansion of an agricultural undertaking. All this sets at a heavy discount the feasibility of really large scale units in agriculture. That is not saying, of course, that large farms, in relation to present sizes, are not economical. It is only saying that largeness on a scale obtaining in industry is not so. That larger units than at present existing do not emerge has to be understood in the context of individual-financial, social, political and other considerations as well. Where such impediments do not exist, whether it is land tenure inadequacies and idiosyncracies, or stress of population, or where they have been overcome, as in certain advanced countries, the tendency has been towards large scale. The plantations as well as the Collectives both stand evidence to it. Even where such conditions do not obtain, given an enlightened outlook, the recognition of the large scale has manifested itself in appropriate fields—the efficient co-operative system of the Danish economy is an outstanding example. The disadvantages of more difficult credit and stiffer conditions whether with Banks or with dealers, the smallness of the entrepreneur (unless coming under share cropping or some such arrangement) and the burden of mortgage loans for development as against share capital in industry, all limit expansion.

On the legal and social sides, there are the systems of inheritance duties and the pride in ownership, which would further raise the price and keep small farms definitely small.

( vi )

One of the most significant features in agriculture is the inflated role of the *Middleman*. Chiefly by virtue of the small-scale organisation relatively to industry, he finds himself obtaining a much greater importance than in industry. He performs sometimes many of the services of assemblage in bulk, grading, processing, storing, transport and actual final sale. It seems that the distribution process takes an alarming proportion of the amount the consumer pays. That distribution should cost more in agriculture



is inevitable. "The small scale of agricultural production, the wide dispersion of producers, the variations, both in quantity and quality of output, and the perishability of the product, all add to the costs of distributing farm goods. These difficulties generally out-weigh the advantages given by the greater stability in the demand for food, which is a type of product less liable to fashion changes than are most others." Yet these costs could be much less. It has aptly been remarked that the danger in wholesaling is mainly excessive profits (through a semi-monopoly) while in retailing it is excessive costs (from overlapping etc.). A further difficulty in marketing, is that consumers' preferences for particular types of agricultural products, as shown by the relative prices they are prepared to pay for them, are often not fully reflected back to the producer in differences in the prices they receive for particular varieties." The chief means towards reducing these excessive burdens has been through consumers' credit and producers' co-operatives. Under mixed farming, or where marketing amounts only to local transactions in a country district, producers' co-operation is not a success. These are among the main reasons for lack of success of producers' co-operation in Britain. As for illustrations to the contrary, there are innumerable in Denmark, New Zealand, California and other parts of the U.S.A., China India and Ceylon. In the last three, the low incomes make the part played by co-operative credit crucial in reducing the burdens brought on by 'competitive' marketing.

( vii )

A fundamental question about agriculture is its *Ability to Earn the Income* necessary to ensure the desired standard of living for all. It is interesting to read a statement on U.S. agriculture to the effect<sup>1</sup> that the basic problem and point about agriculture there has been low income. It is known of course that, as incomes increase, the demand for food will rise, but less than in proportion to the rise in income.<sup>2</sup> The demand for non-food agricultural

---

1. J. W. Schultz. Agriculture in an Unstable Economy.

2. Higher agricultural incomes are generally accompanied by increased consumption on the farm. On the other hand, the elasticity of demand for income in terms of effort may not cause higher income trends. c.f. Silcock in the Economic Journal, June, 1948, Page 229 with reference to the Malayan small-holders in rubber: "Outside labour will often share the proceeds on equal terms with the owner, the latter being compensated by doing less work."



products, will probably increase as much as for industrial goods. But the importance of this in the category of general agricultural produce, taken as a whole, is subordinate. Further, as incomes rise, while consumers will pay more, the amount paid to farmers will not rise as much—marketing costs will rise for various reasons. Again, as economic development proceeds through improved technique and so on, if the latter is in industry, the result will be lower prices in industry but relatively higher in agriculture. The greater demand and diminishing returns will account for the result, unless technique effects cost reductions in agriculture directly or indirectly. Quite apart from prices, owing to the actual immobility of factors, agriculturalists would not have changed their occupations rapidly enough. Agricultural incomes remain lower than industrial. From the point of view of a particular country, other factors, too, adversely affect agricultural income. Among these are changes in transport-technique and cost-benefits to large scale cheap food from abroad. It has been said that “such developments . . . can only permanently damage a country if they affect the things it *sells* to other countries,” and that farmers and workers could turn to other comparatively more advantageous occupations. This assumes of course that the scope for such a change is there and that it is economic. This is a very important point and it will occupy our attention considerably in the later chapters.

( viii )

If such are the general trends, the *Fluctuations* are even more remarkable. In the first place, marketing charges become very stable and constant. The general tendency is to sell at a lower price but not less quantity. Prime costs are more important in marketing and agencies concerned often deal in several occupations and not agriculture alone. Thus they do not have rates related solely to agriculture. Besides, much of the marketing is done by monopolistic organisations. (‘Economic Colonialism’ for raw materials is one and probably among the more potent manifestations of this). In the result, demand becomes even more inelastic and fluctuations of income more marked. As an example “suppose farmers receive initially 50% of the retail price. If this price falls by 5%, from 100 to 95, then the farm price will also fall by 5 from 50 to 45, but this will mean a decline of 10%, twice as



great as the percentage fall in the retail price." There is a convenient example given by Cohen. The retail price of potatoes varied from 264/- in 1924-25 to 142/- per ton in 1929-30 (86%), but the margin between retail and growers' prices was 97/- in both years, and the latter varied really, therefore, from 167/- to 45/- a difference of nearly three times the minimum.

There are seasonal variations, annual fluctuations and cyclical fluctuations, and the general agricultural cycles with their varying degrees of importance and relevance. Some salient points may be noted in principle. In addition to mere fluctuations, when the crop is small, prices open and remain too low, until later a shortage becomes apparent, and prices shoot up; and vice versa. It forms part of the phenomena illustrated by the Cobweb theorem for agricultural commodities. It is the result of lack of adequate information and is one of the reasons for general State intervention in the marketing process in agriculture. We may also note, however, that while yields may fluctuate heavily in countries individually, for the whole world they rarely exceed slight oscillations. On the other hand, local supplies still have a greater proportionate influence for various reasons, including cost of shipping, preferences and imperfect competition. So that fluctuations will be more prominent than the global situation may justify. If the variation in crop yields is sufficiently great and consumption demands sufficiently inelastic it may be worthwhile to store a good proportion of the bumper crop to offset the short crops of the next not merely one, but two or three years (as in coffee). As has been observed "the actual return to the farmer will be greater or less for a larger crop than for smaller according as the elasticity of merchants' demand is greater or less than unity. . . ." So elasticity of consumer demand needs to be considerably greater if the producers are to be as well off when yields are good as when they are bad. If demand is "inelastic, producers' incomes will vary from year to year with crop yield." That has been one of the major problems of agricultural countries and the reason for so many Schemes and Controls, more of which later. It seems also that farmers act on present conditions and often thus lead themselves into a cumulative error of over increase or over decrease of output. It is reinforced by the continuous producing of these new units (cattle, or trees) and it assumes, through the price mechanisms, finally a cyclical



pattern of self-perpetuating over or under production. In between these 'gestation' or 'bearing' periods, however, other exogenous factors, real or monetary, national or international, may, of course, enter at one stage or another, to 'justify' the status quo and thus reverse a disastrous trend, or further to intensify the disaster.

When the length of the cycle varies from product to product, it seems illogical to expect a general agricultural cycle as well. Yet that seems to be the case. It forms part and parcel of the general trade cycle. Whether a fall in agricultural incomes affects demand for industrial goods and induces depression, or whether lowering of costs (through low agricultural prices) to industry stimulates industrial development, is still a moot point. On behalf of the latter, it can be said that by helping to keep down demand for wage increases it operates strongly as a favourable lever. The contention, for example, that in the U.S. agricultural produce constitutes only one-fifth of the total value of output, does not appear to rob it of its influence on trends, both in its own right and by its more subtle and very important influence on wages and costs. However all this may be, the effect on agricultural incomes is only too conspicuous. In the wide fluctuations of national income between the booms and depressions, the effect on agricultural income was clear and marked and was greatest where marketing costs were largest as in Australia, South America, etc., and in which long distances were involved. The demand for food may fluctuate less than for industrial products, but incomes or prices change far more for agriculture and less for industry. So the agricultural cycle is, as has been well summed up, predominantly in prices and profits, and not in output. In the case of industrial raw materials, one should think, the demand too fluctuates as much, and the effect on price fluctuations must be even worse. In several cases, the fluctuations can be bad enough to become questions of inadequate national incomes, problems not of variations but of quantum itself, involving a self-perpetuating backward economy. Of course, since output is rigid (taking even the mid-length period) and costs largely slow to react, "shortages or abundance in the means of payment" particularly affect agriculture. It happened in the periods 1850-70 (of rising agricultural prices) and 1875-95 (of low prices). In a similar state of affairs of the means of payment and industrial difficulties due to ravages, deple-



tions, bottlenecks and costly food, industry itself may be unable to increase output. Then it is bound, as it has been after the second World War, to experience similar effects on its products. But the circumstances, as far as industry is concerned, are exceptional and, to say, generally, that it is agriculture that experiences the wider fluctuations of price and income is, one should think, a fair statement.

(ix)

The amount and nature of interference by *the State* in economic development in agricultural countries will be taken up at a more appropriate stage later. At present, certain points may be made by way of bringing out the degree of imperfectness in an agricultural set-up. Among these are systems of land tenure and inheritance, often the small scale nature of the occupation and the unavailability of 'external economies', inertia, relative immobility and pressure of population, violence of price variations and, not the least, the social factors. They all point conclusively to State intervention. There are various types of ownership. In most countries, the tendency is to break up land into small units. The attendant problem is one of capital starvation. There are also large estates given out on tenant basis. They have numerous variations in rights and conditions as between countries. The State may be involved in encouraging one or the other and remedying defects by assistance as well as by compulsion. It may also look after factors needing a long term view, like soil conservation, research, crops, drainage, credit, marketing and so on. Or the State may plump for Nationalised farming, or Collective farming or a combination of collective and private farming, etc. The State can go, and often countries have gone, further by helping transference of resources from one agricultural crop to another. Instances are the diversifying of agriculture in the West Indies and in the American cotton belt. It can also introduce further diversification by introduction of industry, as and where conditions favour.

Price stabilisation as a means of raising agricultural prosperity constitutes one of the major purposes of State intervention. It is necessary, however, that the result must be a stabilisation of real income and not merely monetary. A distinction has to be drawn



between wanton restriction of output and control of supply of produce brought to market (which means holding over now as well as increasing later, according as circumstances demand). Unnecessary fluctuations, especially if they cause variations in intended output, can have disastrous results. In so far as there is ignorance of the true positions, the State can play a great part both by providing the necessary macroscopic view and by schemes for carrying over surpluses. The latter involves storage. Credit has been a great difficulty in this. The State, or a Farmers' Organisation, can buy up and later sell actually at a profit. Yet, in spite of the apparent simplicity of these devices, as Cohen has aptly put it "it is very doubtful however how far these conditions are fulfilled in practice, especially when the responsible authorities are representative of producers alone. Experience has shown that such bodies are very unwilling to recognise that the underlying conditions require lower prices and are apt to interpret every decline as a temporary one even though in fact it may be due to permanent changes such as reduction in cost of production." The general result is "an unjustified increase in production and a greater price fall than would otherwise have been necessary". This happened with the Canadian wheat pools in 1928 and (through bad luck in part) with the coffee valorisation in Brazil. The inherent failings appeared with the advancing of too much to producers on their bumpers and stimulating over-planting, making collapse in any case certain. While the efforts refer to stabilisation, in practice almost every case has resulted in price raising, as in the well known rubber control scheme in South East Asia. Of course, that is not saying that these variations from the 'long term norm under competitive conditions' was, therefore, a loss or a harm to world or to national economic conditions. That will be discussed and decided later. There is however a lot to be said for the argument that the State should leave such matters not to producers' organisations, but to an independent non-sectional body.

Subsidies to agriculture have been a common method used for various purposes, from controlling price cycles to stimulating consumption. The effect on output, especially in the short period, is dependent on whether the subsidy is for all farm products or only a few. If a subsidy is meant merely to raise incomes but not output it will be granted only to a specified quantity of output. It means,



however, shutting out new competition and its usual assumed benefits. A great point about subsidy is that the burden is on the taxpayer chiefly and not on the farmer as such or on the mass of the consumers living on poor standards.

Import restriction by tariffs and quotas have, also, been tried. Tariffs (unless the country's import demand is inelastic) and quotas both create a market for home production. In the one case, they assure non-competitive higher prices, and in the other, they operate through the fact of the limitation itself. That the effect is to raise the cost of living, and thus lower the standard, is implicit. Its modus operandi is chiefly by affecting the poor who, especially in agricultural countries are badly off already, and who in any country must be the main consumers of the cheaper imports. The curtailment of purchasing power involved in this can adversely affect other home produce like mixed agriculture and industries, inaugurated or existing.

Finally there are the Restriction Schemes controlling supply through price and quantity regulation. This policy assumes for its success a given low price elasticity of demand. On strict economic principles, large waste is involved either in the form of units working far below the optimum level or through waste of part of the product, or both. As has been stated by students of the question, 'the absurdity of the situation needs no stressing'. The practice of dumping is not exempt from similar objections. The stabilisation of prices and avoidance of exploitation of conditions of agricultural supply by world demand, general or industrial as the case may be, are, of course, very important points. The remedies for this and the degree of planning necessary will be considered later. Here we may note that several of the failures of planning in agriculture are largely born of the sectional bias in them. The rapid adapting of the Danish system to the changing conditions at the end of the 19th Century is an outstanding example of the success of planning of the type we have in mind.

( x )

Enough has been said of the economics of agriculture to give an idea of what to expect in the economic background of the



agricultural countries as well as in their economic problems. Before we close the subject, a more specific reference to *Agricultural countries*—the nature of the ordering of their resources as we find them and their implications—will be very useful.

Agricultural countries, by their nature, are primary producing countries. Their earnings are not as much as per comparable unit of industry. Even if they were so, several causes, social and historical, relating to the immobility, mutability and size of factors and their proper combination and exploitation, have, even for countries with scarce populations and abundant land, prevented the optimal combination of factors in agriculture. It is also clear that in population pressure countries, with fragmentation, subdivision, indebtedness et hoc genus omne, the point is so obvious as not even to need demonstration. Where these have been rectified, as in Denmark, or where the population is definitely scarce, the per capita income and the standard of living, have been proportionately high. In other agricultural countries, the position has been stark under-employment and subsistence living. Those are problems by themselves and we will take them up again later. There is also the point that, irrespective of demand and allied aspects of the economic situation, incomes real and monetary fluctuate for natural, climatic and general economic reasons. Especially in the absence of some other occupations of a more stable nature, the results can be highly disconcerting to the economy. The agricultural country depends for other necessities and semi-necessaries on imports and payment in return can be only by export of agricultural produce. This, the nature of the imports and that of the exports have both wide and serious implications for the agricultural country.

The export trade of agricultural countries consists, mainly, of the great staples of diet for human consumption and the vast raw materials that go to feed man and machine. Now what is the position of these agricultural exports in international trade and how much do they secure to the national economy? That they secure big incomes has not been disputed. That they can by themselves secure the necessary imports, secure stability and soundness of the economy and ensure a standard of living, have of course, not been conceded. Wheat, rice, tea, coffee, sugar, jute, cotton,



coconut, rubber are among the prominent commodities on one or more of which the various agricultural countries depend for the sustenance of their economies. (In certain countries, mineral oils, too, play an important part.) In some agricultural countries like Ceylon and India, even the staple diet has to be supplemented, often to a large extent, by imports. If, as in Ceylon and Indonesia, there is also a virtual absence of local industrial goods, the dependence on their other agricultural products becomes even more complete and the foreign trade of the countries occupies a dominating position over the economy. We have seen that the nature of production of these commodities is such that supply, except in the long period, is price inelastic. At the same time, it has been evident that the demand for them is also relatively inelastic.<sup>1</sup> Placed in this situation, agricultural countries have found themselves struggling persistently with terms of trade which, in a different economic context, would certainly have been better. It is a general observation about agriculture that while its output is (relatively) stable, that of industry races up and down.<sup>2</sup> This applies not only nationally but also internationally. The effects must be reflected in the terms of trade. Part of the reason is due to the large and varied middlemen's services being in the hands of other advanced countries; part is also probably due in several cases to the political subjection of the countries concerned. In any case, the countries get (in terms of the 'transformation' theory) much less imports than is likely to be represented in the labour and resources put into the goods exported. Restriction, 'assuming the absence of competition', apart from perpetuating uneconomic units, and therefore waste of resources in the economy, is also not bound to ensure any higher total net revenue than what the 'consumable' output would yield. Any proposition based on the theory of comparative costs, that the solution for any economy is to concentrate on its 'advantageous' occupations, to wit the agricultural exports in our case, is only bound to worsen the situation and incur even a smaller total net revenue than before to the country.

---

1. To lower output, e.g. in rubber, sufficiently and thus raise price without lowering total returns, is, in the nature of things, most difficult.

2. c.f. e.g. Schultz. *Agriculture in an Unstable Economy*. Also U. N. Public. *Relative Prices of Exports & Imports of Underdeveloped Countries*.



Over and above this unpleasant difficulty, the constant embarrassment of marked fluctuations in prices and incomes, caused by factors enumerated earlier, combined to make any long term stability or planned prosperity impossible in the typical agricultural economy. So that the economics of agricultural countries in its 'unaltered' state has been a picture of repeated and sordid results. To the extent that there are some industries, the ill effects tend to be mopped up. But the trend is not altered. Nor is the position different in population-scarce countries with the higher standards of living, except, as said earlier, the ability to have more effective Social Services and Insurance Schemes for depression.

Certain other points too may be recapitulated. The propensity to consume is high, the rate of capital formation is low, absolute quantity of capital in the economy itself being quite small. There is hardly any equivalent to what would be understood in an integrated economy as the stages of production. There is a consequent relative shyness and especially inefficaciousness of capital in solving the overall problem of full employment of men and resources. Non-durable imports increase with every increase in internal purchasing power.

There is overwhelming prevalence of sub-normal incomes and only nervously stable other incomes. There is risk of higher tariffs affecting cost of living seriously, and a limitation of taxable capacity as well as general lack of buoyancy therein. In brief, these countries are peculiarly dependent on world stability for their standard of living, and on extraordinary world prosperity for even a slight increase in that standard. It is fairly clear that they have to seek a way out. There is also the duty of helping world stability, by themselves jointly devising and maintaining prosperous and stable standards.

( xi )

Generally speaking, the *Solution* to the problem of unemployment, a low national income, depression, has been located in adoption of the objective of full employment and worked out in the theory of employment. It will be well to set out the salient points of this theory and the economics of it, in order that, later, we may better consider the extent to which the peculiar character of agricultural economies will require particular alterations or adaptations in the generally understood concepts.



## The Theory of 'Full Employment'

(i)

THE subject of the means to full employment has had a chequered history, ending up only in recent years in any general consensus of opinion in favour of a particular theory. The notion of full employment level as the position of equilibrium par excellence to which every economy is naturally tending and in which contrary factors are only frictional forces, was buttressed by the homely principles of the conservation of purchasing power and that supply creates its own demand; this constituted the classical theory. It is not necessary to go in detail into the merits of this theory whose practical irrelevance in the above form has now ceased even to be controversial.<sup>1</sup> It saw the remedy in increasing savings and thereby enlarging investment, having, of course, located the evil in inadequate savings and (by implication) a constant tendency to excessive consumption or non-investment activity. If over-investment was talked of, it was not as the obverse of under-consumption, but of under-saving. It is now accepted that the factors relating saving to investment are not the same as those assumed before. In fact, the function of the rate of interest is not to equalise saving and investment, for saving always equals investment, and is so equal by definition. There is, of course, a distinction one would like to make between productive and un-productive investment and establish, if one may hazard it, a correspondence respectively with saving and hoarding. However, for the present that is by the way. What is more important to note is that there is, must be, some relation between production and consumption. As is now well accepted, there is no case of supply automatically creating demand (unless we assume a moneyless, real economy and fully diversified and perfect complementarity of structure—which latter is really going a large way towards assuming full employment, and so begging our question itself). In these circumstances, large portions of purchasing power, whether through

---

1. This is not to deny that several 'classical' concepts still hold good.



psychological and personal motives, or for business and other purposes, are bound to be lost, in the all too frictional set up, to effective consumption. This would mean that, in any given state, it is the constant tendency to under-consumption that tends to let the economy sag, to lower and lower levels of activity and employment. If saving is overwhelmingly the function of income, it is logical to argue that, given a drop in the level of consumption, investment and income are soon likely to drop to a level corresponding to that level of consumption. What is more, given these new norms, the economy at that point will be in equilibrium. It is certainly a jolt to a faith in the Unseen Hand. It introduces a devastating truth—for there is no one equilibrium position par excellence, and that makes the ship almost rudderless. If one thing is clear, therefore, it is that the pursuit of full employment and the avoidance of stagnation require conscious control and direction towards a consciously selected target.

The theory does not deny that, in the real world, there is no settled equilibrium at any level. The diverse factors that enter so nebulously into determination of the marginal efficiency of capital certainly would induce fluctuations in the decisions to invest; and, on interaction with the connected propensities to save and consume, would ultimately affect in turn the rate of investment, of growth or decrease of income, and so on. "The cyclical variations which we observe are then explained by the complex interaction and time sequence of investment decisions governed by a multitude of past, present and expected events, which . . . formed the basis of entrepreneurial profit expectations and of saving or consumption decisions depending mainly on changes in the level and distribution of income. Whether such variations will be less or more violent and whether they will occur round a high or low level of employment depends again upon the quantitative and time relationship between the propensity to save and the inducement to invest."<sup>1</sup>

On the theory itself, a pursuit of the steps in economic change would show that, for instance, a given increase in the volume of investment would ultimately register an increase in income that is a logical multiple of this initial investment decision. If the propensities to consume and save are known, assuming an integrated

1. "The Economics of Full Employment" (Oxford Economists) Page 32.



economy, it would be possible mathematically to assert by how much this income would multiply. In a similar way it is also possible to talk of a consumption multiplier. There is also a 'foreign' multiplier, showing increased incomes caused abroad by increased consumption at home, which is for us a very important factor and to which we shall need to come later on.

Thus, as a logical growth from the foregoing, the means to full employment has been indicated and accepted. Put simply, it is that the purchasing power of the economy must be maintained. Apparently, this can be performed in three ways—by creating new work, by stimulating private investment, and by redistributing income. All of these can be further relied on for their secondary and tertiary effects through the multiplier mechanism. The first is the most direct and would be achieved by public works policies, doles, social services and the like. This invariably calls for a deficit budget. The old philosophy of the balanced budget is thus overthrown. In an opposite economic context, that is at a boom level of activity, the principle would be one of surplus budgeting to reduce purchasing power in the economy. This aspect of employment policy has become a vast subject, involving the principles of timing investment and preparing schedules of public investment plans and so on. The second device, that of stimulating private investment, is a potent one. However, a process of achieving full employment thereby is not only an indirect way of adding to purchasing power, but also is likely to lead to excess capacity, reflected, at successive stages, in need for cumulative decrease in rate of interest. The amount of investment which will leave enough purchasing power to keep the economy at full employment level will be excessive. The rate of interest is only one of the factors entering, through the marginal efficiency of capital, into the decision to invest. With appropriations for depreciation, reserves, deepening of capital and so on, even before the capital equipment reaches excess capacity in a physical way, it is likely to be in excess relatively to purchasing power available to absorb its output. These points are not meant to controvert the fact referred to by the authors earlier quoted that private investment must come in at a level "adequate to expand the capacity of equipment *pari passu* with the increase in working population and productivity of labour, i.e., proportionately to full employment output." The



points are made only to confirm that the accepted marginal efficiency of capital will not long obtain (despite inducement through the rate of interest or income tax) unless purchasing power is directly fed. In the former the inducements must be cumulatively supplied ; in the latter, the inducement gives investment itself an indirect cumulative effect. So that, in a sense, the proper inducement to invest is an inducement to consume. That is till investment and employment reach the required high level, when the financial and fiscal policies will be adjusted, or reversed, accordingly. There is then the third device, which would also seek directly to supplement purchasing power. In the absence of the old inhibitions against taxation as being inimical to production and full employment and in the context of accepted Social theories, re-distributive taxation falls logically into the budgetary system. It transfers incomes to the classes whose propensity to consume is greater. Taxation at certain levels may, however, be at the expense of consumption. To that extent the fillip to employment given by re-distribution of income is likely to be less. Without abating the use of taxation to the optimum level, the greater reliance is, therefore, for this and allied reasons, placed on deficit budgets by loans related to Public Works programmes and Social Services. As a reasonable summing up, we may repeat the conclusions of the architect of the theory, that while the cure lies more in maintaining consumption, since, at the core, unemployment is due to a deficiency in consumption, still the most practical and wise policy lies neither in merely stimulating consumption or investment, but in a judicious advance on both fronts, . . . shall we say, till the rate of interest is zero. The control required for such advance is to be secured by investment boards and public works policies. We must not forget the central contention, however, that in a given set of relations at any given time, the cause for a low level of employment is (apart from immobility and allied frictional factors) under-consumption or demand deficiency.

( ii )

It is not intended to question the theory itself, relating as it does, to certain problems that are matters of fact. The old confusions and contradictions of various and opposing theories on so many subjects in the field of economics, born often of a vagueness of



terms and differences of emphasis and overlooking of the assumptions, have been only too common.<sup>1</sup> It is not necessary to revert to that harassing state of opposing a theory, when the difference is really one of emphasis and context, and to perpetuate the easily earned reputations about the vagaries and unreliableness of economic theorists, so often, in the past, unable to agree among themselves, nor to have the confidence of the framers of State policy.<sup>2</sup> If the assumptions of that theory, as well as the context in which and for which it was framed, (and the various emphases), are overlooked, then any alterations we should pose are bound to appear as completely alternative, possibly opposing theory. The theory of employment as accepted today is not disputed. What we here set out to cast aside is chiefly the means to that employment as worked in the more advanced economies.<sup>3</sup>

For one thing, it is evident that the various means to full employment hitherto analysed, have an eye more on the maintenance of the general level (or trend) of activity, that is the avoidance of the cycles of boom and collapse,<sup>4</sup> than on the rescuing of an economy from an already existing unsatisfactory state of equilibrium. The latter is the case in depressed countries whose state may be described as one of full employment under under-employment conditions. The relative insignificance of the inducements-to-investment proposal, as one of the means to full employment,

1. c.f. The passage from page 297 of *General Theory* quoted in the preface to this thesis.

2. c.f. *The American Economic Review*, May 1948, Pages 291 and 292. L.V. Chandler "The present period of inflation in no way refutes the basic Keynesian theories. ... The present situation can itself be explained in Keynesian terms. ... Keynesian theory shows its usefulness in dealing with both types of situations—a high rate of investment relative to the propensity to save as well as a low rate of investment relative to the propensity to save". c.f. e.g. Page 273 of *General Theory* "—in conditions of full employment ... a low propensity to consume (is) conducive to the growth of capital". c.f. also *General Theory* Page 48 "It is not necessary that the level of long-period employment should be constant, i.e. long-period conditions are not necessarily static. e.g. a steady increase in wealth or population may constitute a part of the unchanging expectation. The only condition is that the existing expectations should have been foreseen sufficiently far ahead."

3. The point could in fact be inferred from a statement in the *General Theory* (Page 125) that the 'full employment devices' will have an uphill task in poor countries—"For whilst a high marginal propensity to consume involves a larger proportionate effect from a given percentage change in investment, the absolute effect will nevertheless be small if the average propensity to consume is also high."

4. c.f. *The American Economic Review*, September, 1948, Page 563 Patinkin—"Keynesian theory acquires meaning only when applied to systems with more intelligent monetary policies."



in existing theory, is evidence of that placement of emphasis. The theory has discovered, and clearly stated, that there is no one equilibrium level par excellence. The state of certain agricultural countries is one level of equilibrium—however procrustean it be. Having stated that, however, the theory has proceeded, in discussing means, to consider only a level of equilibrium familiar in advanced countries and to discuss how fluctuations round that may be guided to produce stable progress. In inferring the fact of demand deficiency, it would appear that a certain level of productivity and output has been assumed in the first instance.

It would be clear that the problem of full employment in agricultural countries is not a problem of guiding fluctuations round a given level of equilibrium and pressing them down to form a neat trend (for which even the devices of maintaining purchasing power is, as we shall see, so unsuited). The problem is one of getting on to a completely different level of equilibrium. The term equilibrium conceals the fact that, in agricultural countries it is but a theoretical expression of what we should otherwise call a vicious circle—of depression and more depression. This brings us to the vital assumption on which the full employment devices have been, implicitly or otherwise, based.

The General Theory of employment, being a statement of what generally obtains in the advanced countries, has assumed the characteristics of their economic background. Of these, two stand out as vital constituents. The economy is assumed to be well integrated in respect of its several stages of production; and secondly, it is also assumed to be fairly diversified. It is widely accepted that for an initial impetus, either in the form of investment or addition to purchasing power direct, to produce an ultimate multiple income, the series of 'connections' between this initial point and the end must be fairly closely related and sensitive to the movements and fluctuations of one another. As a rule, and for practical purposes, it will be necessary for the various stages of production to exist within the economy and for the mechanism by which these stages are related to be well lubricated. It means that the stages must be fed by a smooth and ready credit mechanism; that they must, in their organisation and methods, be advanced and large enough to perceive the change appropriately, and



possess the technique to step up production ; and that the distributive channels and costs should serve rather as a help than a deterrent. It is really doubtful, in countries like India and Ceylon, how much a given noticeable addition to purchasing power of the Keynesian type can produce the anticipated increased output. Probably, that is not disparaging the theory at all, for, in discussing the problems of Prices, Keynes himself had elaborated the assumptions and bottlenecks and drawn the appropriate conclusions. In less advanced countries, with no adequate money market and other money sources, and the various technical and economic imperfections with which production is so pre-occupied, the only result of any considerable 'inducement to consumption' may well be rising prices.<sup>1</sup> With agriculture dominating so much in the economic set up of backward countries, to talk of the existence of integrated structures would be unrealistic. In any economy, integration is not always so complete as to comprise all the stages of production from start to finish, even though the stages that exist may be quite closely knit.

In industrial countries, the raw material stages are predominantly absent ; in agricultural countries those are about the only stages significantly present. Considering the inertia, the artificial encumbrances and the dependence on extraneous natural factors, it is only to be expected that what integration there exists in agricultural countries is far less responsive to stimuli by full employment devices than integration in the 'industrial' stages.

For the sake of clarity, the concept of integration might be further briefly elaborated. A consumption good at the retailer's counter is naturally the category able to point to the largest number of stages of production that must have preceded its final output. (This is the sense in which Keynes would probably have it in the General Theory.)<sup>2</sup> It does not follow however that all the stages preceding are within the physical boundaries of the economy concerned. In agricultural countries, the earliest stages and

---

1. A similar point with slightly varying emphasis is that made by Hicks at Delhi University in February. In a purely manufacturing economy "manufacturers .... were reluctant to raise prices until their costs changed. The expansion so long as it proceeded at constant money wages would also proceed at constant real wages". But in the agricultural economy "increased demand would raise prices even before wage rates rose".

2. c.f. Page 287 on the period of production.



sometimes the middle stages are absent. To take even a favourable case like rice, in so far as tractor farming becomes now essential, the 'higher' stages are outside the frontiers. In the case of rubber and coconut, the middle stages, i.e. those between the early raw materials and the final consumption stages are absent. Now no country has all the stages of all the categories within its boundaries. So that, by lack of integration we do not mean any such deficiency. There is no reason why far more of processing stages in raw materials industries should not be undertaken by these countries and even several of the capital goods stages in cases like India. These are entirely different points and not directly relevant here. But the inability within an industry, for an increased demand on its output to be readily translated into increased supply, would certainly point to a lack of integration. The exact point at which the deficiency exists may again vary. It may be lack of tractor output for rice or trawlers for fishing or machinery for textiles. But it may be also something else equally important. For, within the framework of whatever stages exist, there may be no financial or organisational integration to produce a suitable linking of demand to output. Poverty of investible resources and more especially the ideas on liquidity and terms of credit, the lack of that steady flow of capital from industry ploughed back annually into itself, the general lack of co-ordination in supplies for production, in transport and in manufacturing, are among the features of backward agricultural countries. They mean, in other words, lack of integration in the structure. In a situation such as this, mere strengthening of purchasing power is inevitably far less relevant than in the advanced countries.

As for the second assumption, that there is a fair degree of diversification in the economy, the very nature of the agricultural countries would exclude them from this category. It is apparent that any given addition to purchasing power is spent not on one commodity but on a variety of commodities. Thus the greater the degree of diversification, the greater the realisation of the benefits of full employment policy. The consumption of food and other natural products, for which demand is relatively inelastic, is at a high level. Any incompleteness of diversification in industrial countries is far less likely to prevent the operation of the multiplier effect, than a similar incompleteness in agricultural countries. This is further



underlined by the fact that most industrial countries also maintain a certain proportion of agricultural output. That is not to say that the export multiplier does not operate significantly in industrial countries.<sup>1</sup> But the question remains whether the respective leakages of the multiplier in industrial countries and agricultural countries are comparable at all. Even the degree of diversification in their agriculture is small in most agricultural countries (some specialising in cereals, some in dairy produce, some in plantation produce or raw materials, some in vegetable and garden agriculture, but rarely in any variety of these). The consumption of 'food', in relation to other items in the household budget, is at a high level. An addition to purchasing power is, therefore, likely to produce a pronounced leakage of the multiplier abroad.<sup>2</sup> Nor does this cause a proportionate increase in world demand for agricultural produce and full employment, thereby, in agricultural countries. The conditions of elasticity of supply and demand are unfavourable to this. If one may use a devious converse of the term, there is no compensating leakage of the multiplier *in*. In the absence of the balancing of the respective leakages, 'out' and 'in', the balance of trade is bound to be tipped adversely. It would amount to saying that the lack of a judicious and proper diversification<sup>3</sup> in the economic structure is the first cause in the set of relations inducing an adverse balance. Hitherto,

1. c.f. General Theory Page 120 "if we consider only the effect on domestic employment (as distinct from world employment) we must diminish the full figures of the multipliers." Another instance of the general validity of the Keynesian thesis, in spite of the irrelevance of its particular interpretations in policy-decisions so far. The point is elaborated further by him in Pages 121-2.

And again Page 262 "If we are dealing with an unclosed system, and the reduction of money-wages is a reduction relative to money-wages abroad....it is evident that the change will be favourable to investment, since it will tend to increase the balance of trade."

2. In the long run, of course, the adverse multiplier effect in foreign trade is bound to be arrested and even compensated—either through exchange or quantitative restriction or both. However it will be at the expense of being satisfied with existing standards of living and states of employment and doing away with the idea of a Social Service State!

3. It was not denied that an increase in purchasing power could cause some small increase in food consumption, although the larger manifestations of a substantial increase in purchasing power, would be in respect of manufactured goods. Even this, in the case of Ceylon, is irrelevant, because the overwhelming proportion of the food is imported. In India, one may talk of a direct incentive for the purchasing power to stimulate internal agricultural activity. Whether it would really produce any results is, however, again doubtful in view of our point about 'integration'. The lack of this amounts to a lack of organisation. We could, probably, speak of lack of both integration and diversification as first causes—or, lack of economic organisation and of capital investment. All of which, however, more later.



more than half the world's population was left outside the pale of theoretical study. Except for vague propositions regarding development and capital exports from surplus countries, they were left unserved by any theory of employment and left to build their actions without any special theoretical frame-work or foundation.

By diversification, it may be mentioned, is not meant an indiscriminate range of units of production. In the first instance, it is not a concept referring to a vertical set up in the various lines of production. A hundred Units of production all in one or two lines of production is not diversification. But a hundred Units (significantly large) in a dozen or more lines is diversification. The ideal state, shall we say, is to have both integration and diversification, but the one is different from the other.<sup>1</sup> One definition of diversification runs as follows : "steps to diversify national economic activity for the purposes of distributing employment eggs into several baskets, of resisting the downward tendency in the bargaining position of the producer of food stuffs and raw materials against countries exporting manufactured products, and of increasing national economic power". This . . . would include agricultural diversification, introduction of light industry and even heavy industry.<sup>2</sup>

To recount, therefore : The classical notions of the rate of interest, as the regulatory factor of the economy and as sufficient inducement to reinvestment and recovery after a slump, does not reconcile with the non-self-adjusting nature of economics as observed in their working. The role of the interest rate is even less significant in agricultural countries. The alternative notion of inducements to investment, both by strengthening purchasing power and influencing marginal efficiency of capital, is far more realistic and acceptable. Still, the 'devices' for full employment, as worked out hitherto by theorists, represents, in so far as agricultural countries are concerned, at the least, emphasis on the wrong aspect of the general theory and its set of devices and, at the worst, a catastrophic substitution of a useless theory by a positively harmful one.

1. c.f. *The Economist*, January 28th, 1950, Page 178—From the experience of advanced countries, too, certain queries have begun to be raised—e.g. what if employment is due to inability to pay for necessary imports of raw materials; or to real distortions either in the industrial structure or structure of wages, prices and costs. "Is it right to believe that, given the maintenance of effective demand they will correct themselves?" Also c.f. *The Economist* of June 4th, 1949, Page 1026.

2. Buchanan, *Economic Journal*, December 1946, Page 539.



However, we do not need to go so far as the latter standpoint, though this will help to emphasise that, sometimes, a wrong conclusion is as dangerous in practice as a wrong theory. It will be more useful at this stage, having judged so far the irrelevance of the general theory to agricultural countries, to express the relevant policy in Keynesian terms.<sup>1</sup>

It has become clear that the attainment of full employment level is almost entirely dependent, at least in the first instance, on stimulating investment directly and not in stimulating consumption directly. It means that the aim of full employment has to be worked out more in terms of concrete investment activity, than of mere addition to purchasing power. In common with industrial countries, however, it is accepted that there is no more any sanctity in the balanced budget. The 'euthanasia' of the rentier is also accepted in idea, though not necessarily in practice. For, that depends on several factors like the need, or otherwise, by the state of conscious direction of economic development, the ability of the State to step in and so on—all of which later. In general, it would appear that the Rentier in agricultural countries must not, in the present state, be treated to any 'undue doses' of the euthanasia, at least for the reason that the inducement-to-consumption device for attainment of full employment has been already seen to be somewhat unusable in the agricultural economy. It means that the nature of the Budget in agricultural countries will be somewhat different still. However, while the emphasis is clearly on investment activity, it will of course not be inferred that it is only on it. In a sense, any addition to consumption is related to an investment activity, and, more particularly, any investment activity certainly induces a given amount of consumption activity. So much so that, half way down or up this range, it can be a matter of dispute

---

1. As an instance of the possible range of interpretation of the General Theory c.f. Patinkin, *American Economic Review* September, 1948, Page 564 "The policies would in general be directed at influencing the consumption and investment functions themselves, in addition to manipulating the amount of money. Thus the policies may advocate tax reductions to stimulate consumption and investment or may insist on direct government investment to supplement private investment.

In this way we could cross-classify Keynesian positions according to their advocated policies, as well as their theoretical foundations." c.f. also *General Theory*, Page 325 where the manner of decision on the alternatives are clearly put forward.



whether a particular disbursement represents investment or consumption. Public works of a sort, and especially 'relief' works, are cases in point. It may be reasonable to hold that the decision rests on the nature of the economy where this disbursement takes place. In an advanced country, it may be more appropriate to call it investment, and in agricultural countries consumption. Not that, in the latter, it does not add to the stock of the country's 'created wealth', but, from the point of view of effects, if that is the criterion, it remains more or less only consumption. In other words, the point of the emphasis on investment activity for agricultural countries is that, if one may use what is sometimes a controversial term, disbursement should be on 'productive' investment; and the more highly productive, the better. As for the fear of demand deficiency out of which, in a sense, the general theory was born, it is observed that the investment programme will itself create a given addition to purchasing power. Any further deficiency will be a matter for observation of the development of the economy under such a programme and, if required, strengthening of purchasing power accordingly.

( iii )

Post Keynesian analyses have found certain inadequacies in the General Theory irrespective of any particular economic climate such as we have considered ; they have found the theory wanting in its general validity as a theory itself. One of the findings is that "changes in the distribution of a given total tax burden will not greatly alter the amount of consumption out of a given income". The reason is that the bulk of the taxable income and therefore of tax payments is found in the middle and lower groups, so that only a limited amount of tax burden can be transferred from one income group to another. Secondly, differences in the *marginal* propensity to consume of different income groups are not so great as is frequently supposed. Thirdly, the present revenue structure is already fairly progressive. It is, in fact, recognised that anti-deflationary measures may also take the form of tax reduction. Yet another point is Keynes's under-emphasis on the price aspect of monetary changes. While it could be ignored in depressions, in practice Keynes' volume of effective demand, adequate to give full employment, produces cost-price effects that



are unstable for the economy. If so, Keynes's stable equilibrium is not at full employment but something short of that.<sup>1</sup>

It is doubtful, however, whether all this is not more a question of suitable adjustment of the Keynesian system than of a plea for an invalidation of it. After all, the fundamental change of emphasis from the neoclassical atomistic analysis to macrocosmic quantities, especially the concept of income, is crucial and is Keynesian. The same opinion could probably be held in respect of what follows.<sup>2</sup> The arguments herein are, however, important and we shall set them down in greater detail.

Keynesian theory did not really make any elaborate contribution to the theory of economic dynamics, though it did mark a considerable advance from the previous static principles.<sup>3</sup> Historically, for example, it has been pointed out that the rise of the automobile had an effect on national income, evoking a dynamic response, both of consumption and investment, each to the other. The interdependence of consumption and investment in this fashion is, in fact, said to constitute the essence of economic progress.<sup>4</sup> So much so that since 1941 (year of Kuznet's paper on Capital Formation 1879-1938) the 'secular upward drift' of the consumption function has become a standard part of the statement of the consumption function. Further, there is a dynamic equivalent of the cost-price effects, the cost-reducing function of investment, leading to a release of consumption income for other purposes. A higher standard of living is achieved. This is indeed reckoned to be more important than the money income and

1. Note, however, *General Theory*, Page 270—"There are advantages in some degree of flexibility in the wages of particular industries so as to expedite transfers from those which are relatively declining to those which are relatively expanding." But whether it is workable politics is probably the question.

2. c.f. "a theory is only overthrown by a better theory, never merely by contradictory facts"—quoted by J. T. Dunlop from J. B. Conant's 'On Industrial Science'—*American Economic Review*, May, 1948, Page 349.

3. c.f. e.g. The role of expectation in his discussion of the Marginal Efficiency of Capital—Pages 138 and 145.

4. It is also interesting to note the opinion that "any dynamising of Keynesian technique by mathematical methods does not get us much further"—*American Economic Review*, May 1948, Page 281, J. H. Williams. In fairness to the *General Theory* the following excerpt may be mentioned as mollifying some of the new differences—"it is easy to conceive of conditions which will cause (employment) to increase at some stage to a higher level than the new long period employment. For, the process of building up capital to satisfy the new state of expectation may lead to more employment and also to more current consumption than will occur when the long period position has been reached". Page 49. The point is repeated in a later chapter in Page 123.



employment provided by the capital-goods industries on which the investments may be made. The Keynesian monetary and fiscal policies 'as a means of sustaining full employment in an advancing society' have submerged the price-wage-profits relationships. There have been doubts after the War, even on the short-run stability of the consumption function.

At least econometricians seem agreed that the simple relationship of Keynes between income and consumption is unstable. The working out of a better relationship has introduced new propositions in the General Theory, especially the application of liquidity to consumption and not investment alone, and drawing in of various hypotheses like 'saving of past income, liquid assets, capital gains, the last highest income reached in a boom, expectations of future income'.<sup>1</sup> At this point some of the more enlightened pre-Keynesian economists would seem to be winning their due share of credit.

It is no excuse but it can be argued that Models and models could be created, all on Keynesian lines, given varying data. Keynes' analysis in the General Theory is a short-run analysis, explicitly assuming the wage rate to be constant and the stock of capital to be constant.<sup>2</sup> If so, it could be said that, thereafter,

1. For several elaborations of the points raised in these paragraphs vide *American Economic Review*, May 1948.

2. General Theory, Page 109. "In the argument of this book, however, we shall not concern ourselves, except in occasional digressions, with the results of far-reaching social changes or with the slow effects of secular progress. Also Page 146. The introduction of his concepts are referred to as doing away with the static state "whilst reducing to a minimum the necessary degree of adaptation." The problem seems to be, however, that Keynes tucked the innumerable dynamic functions too far away to have salutary restraint when the formation of policy came up. In his own words in talking of Ricardo, he discarded and then forgot—at least several Keynesians did. c.f. e.g. Page 220—when, in the expected generation, the marginal efficiency of capital has reached approximately zero, "we should attain the conditions of a quasi-stationary community where change and progress result *only* from changes in technique, population and institutions..." The use of the word "only" is symptomatic of the emphasis on static theory. Consider again the formidable list of things taken for granted in the re-statement of General Theory in Page 245. Once more, however, a warning quickly follows (Page 247) "The division of the determinants of the economic system into the two groups of given factors and dependent variables is of course quite arbitrary from any absolute standpoint. The division must be entirely on the basis of experience... Our *present* object is to discover what determines *at any time* the national income." In Page 293 Keynes speaks, in connection with money, of a theory of shifting equilibrium—meaning the theory of a system in which changing views about the future are capable of influencing the present situation. To repeat, this concept is nowhere fully used, but it seems almost certain that Keynes would expect to see dynamic economies worked out within the framework of his approach to the problem of employment and incomes.



it is for others to work appropriate models for the appropriate contexts. The important and useful point to remember would probably be that these Models could be extremely divergent and so policy-measures equally varying, even though the modus operandi of analysis be Keynesian.

On the irrelevance of Keynesian theory in the 'dynamic' sense, Harrod's treatment<sup>1</sup> would appear to be more arresting than the foregoing, from our point of view. In the real world, any situation is part of a dynamic problem.<sup>2</sup> Under certain conditions, this fact is brought into even greater relief. Such conditions Ceylon, for instance, may be said to demonstrate in a prominent manner. The disturbance to its static (almost stagnant) conditions is not, of course, through rapid capital accumulation or increase in productivity, but through a more prominent and, in the present situation, less advantageous source. It is what has been aptly termed an unstable demographic situation. Increasing population through high fertility coupled with decreasing maternal and other mortality rates, register their inexorable effects on the economic situation. Unaccompanied by economic development, they, verily, constitute our most expensive hostages to Fortune. It becomes a study, in the words of Harrod's *Dynamic Economics*, of "the necessary relations between the rates of growth of the different elements in a growing economy". "We shall not have a very sound policy if we envisage treating the problem of unemployment ad hoc from month to month without regard to what sustained level of capital outlay is necessary for an advance of the economy in line with what fundamental conditions allow".<sup>3</sup> Harrod enunciates the point that, to a given rate of economic growth, there is a given rate of capital accumulation, which he terms the natural rate ( $G_n$ ). There is also a warranted rate ( $G_w$ ) of accumulation, which would maintain existing production at full capacity. Where  $G_w$  is less than  $G_n$ , it means that saving (thriftiness) is less than is necessary to enable progress to be made. In the words of a review of Harrod, if population is increasing, the stock of capital will be growing more slowly than available labour, while

---

1. c.f. e.g. his *Towards a Dynamic Economics*.

2. Note Harrod's statement elsewhere that the Trade Cycle is only part of Economic Development Theory (*American Economic Rev.*)

3. Pages 19 and 74.



the amount of employment associated with a given stock of capital is continually falling as technical progress takes place, so that there will be a progressive increase in unemployment. Here we cannot avoid history, for the amount of unemployed at any moment will depend upon how long this process has been going on. This unemployment is not susceptible to Keynesian remedies, (or rather, the normally understood Keynesian remedies). If the level of effective demand were boosted up, for instance, by putting some of the redundant labour to work on public investment schemes, the demand for consumption goods would be raised above the capacity output of existing capital equipment. An inflationary rise of prices would set in. In the case of Ceylon, the inflationary trend is not likely to be excessive ; rather, the effect will be prominently manifested in an adverse balance of payments.<sup>1</sup>

It may well be that, in India and Ceylon, the seemingly irrepressible adverse trends in the balance of payments in 1948-49 and probably again in 1952 are a reflection of disbursements of purchasing power to the population. An authoritative statement on this point should require much more statistical examination of the pertinent sectors of the economy and cannot, certainly, be established by a process of deductive relations alone. Our conclusion, however, is very likely to be true and it may be well worth it for the country to go further into its verification.

The foregoing may come as a shock to those who had the facile impression of a particular theory having a general validity in its application; or who were not aware that any major variations were at all possible. Let it be noted, however, that, in supporting this case for more 'thrift', we were not going back to the analysis of nineteenth century economics, although we may be endorsing some of its maxims. To what extent 'thrift' can be increased without infringing too seriously on consumption, in an overpopulated back-

---

1. c.f. e.g. Harrod Page 88. "Saving is a virtue and beneficial so long as Gw is below Gn. While it is disastrous to have Gw above Gn, it is not good to have it too far below, for in that case, although we may have plenty of booms and a frequent tendency to approach full employment, the high employment will be of an inflationary and thereby unhealthy character." Page 91 "There are two distinct sets of problems both for analysis and policy, namely: (1) the divergence of Gw from Gn; and (2) the tendency of G to run away from Gw. The former is the problem of chronic unemployment, the latter the trade cycle problem."



ward economy, is a point of crucial importance.<sup>1</sup> While we now know that direct subsidising of purchasing power, or even indirect subsidising, when worked on wrong bases is unsuited to be the main plank of economic policy in this country, we are also led to the inference that thrift and investment both need to be planned by the state. Thrift must include foreign borrowing as well.

One thing is clear. As for subsidising purchasing power it must be predominantly by the process of the increasing wages bill for the country from the new industries, which would have been introduced and financed on a planned basis, and not by mere monetary disbursements which, in effect, do no more than raise the demand for goods and services and assume away all the relevant important and vital components of a secure Full Employment policy for agricultural countries.

The programme of Full Employment for agricultural countries will, then, be worked out on these lines, wherein, the 'investment boards' will play far greater roles than 'public works policies'. Put differently, it implies a policy of industrialisation—in the widest sense of the term—and the various implication of such a policy. The fundamental implication is that the best employment policy for agricultural countries is an industrial policy. That this phrase envelopes more ideas than raised above, will be seen as we proceed further with the discussion. Just now, it sets us adequately in readiness for the next part of our study.

---

1. Continually emerging under-consumption (as against a permanent low level of consumption or chronic under-consumption) is a concept quite divorced from the latter. The under-consumption of agricultural countries, it may be repeated, can in terms of existing Income and Investment be of just the right amount for equilibrium. In actual fact under-consumption in the Keynesian sense too is likely to exist in agricultural countries. But while the common malady stems, in advanced countries, from an already existing high level of Investment, in agricultural countries it is directly from a low level. Where the level of investment is absent, the attack on under-consumption by known employment devices becomes quixotic—ineffective through inflation or adverse through the balance of payments—and makes capital even more "nervy".







PART II









## The Term 'Full Employment'

THE term full employment has today acquired a rich meaning which is somewhat different from past conceptions. In the set of relations, however, of the facts and of theory in regard to employment in agricultural countries, as seen in part one, certain component ideas in the meaning of the term may also turn out to be irrelevant or over emphasised. Thus a clarifying of this term becomes essential, not merely to understand its modern accepted sense, but more to define its correct colour and meaning in our context.

Full employment is, of course, a suitable and the desired target. Whether it is equally suitable to describe it as providing jobs for all is, however, another matter. In any case, if that were all the meaning, it should be sufficient to condemn all the past and present governments of agricultural countries as recklessly irresponsible and incapable of seeing a glaring proposition. It is clear that the employment concerned must be productive employment. The mere slogan "employment for all" is not really the same as, for example, the concept of "standard of living" for all. The term full employment has been crystallised in the description that it "means that unemployment is reduced to short intervals of standing by, with the certainty that very soon one will be wanted in one's old job again, or will be wanted in a new job that is within one's powers."<sup>1</sup>

In a sense, there is nothing to quarrel with in such a definition. It excludes, rightly, the margin of frictional unemployment inevitable, not because there are less jobs than the number needed, but because "in every progressive society there will be changes in the demand for labour qualitatively if not quantitatively; that is to say, there will be periods during which particular individuals can no longer be advantageously employed in their former occupation and may be unemployed till they find and fit themselves for fresh occupations."<sup>2</sup> So far the position is certainly acceptable and the best, especially with the emphasis on "having always more vacant

1. Beveridge—"Full Employment in a Free Society." Page 18.  
2. Page 18.



jobs than unemployed men", thus making the labour market always a seller's market. The consequences are promotion of technological improvements, reduction of frictional lags in unemployment and inducement to labour for maximum productive effort in return for the fair basis of 'work for all.' There is finally the vital point that "idleness even on an income corrupts; the feeling of not being wanted demoralises." "For men to have value and a sense of value, there must be useful things waiting to be done with money to pay for doing them. Jobs rather than men should wait."<sup>1</sup>

To the achievement of that level of employment, certain conditions are necessary. At this stage, our difficulties in uncritical and easy application of the ready-made concepts would arise. The three conditions by now familiar to students of the subjects are adequate total outlay, controlled location of industry and organised mobility of labour. The last, for clarity, we may call effective mobility; mobility may be said to be absent, despite physical movement, if some required technical skill or education is absent, and, conversely, mobility present, despite physical immobility, if work comes to one's doorstep. Assuming that frictional employment is reduced to the minimum it would appear that, in a given set of conditions, what would reduce unemployment from, say, 20% to the desired level of 3%, is public outlay by the State. This we may infer to be largely for adding to purchasing power and strengthening of consumption. This would be in line with the theory of unemployment, in so far as demand deficiency is the cause and in so far as the multiplier effect is valid. So that, although the modern concept of full employment recognises the need for mutual adjustment between demand for and supply of labour qualitatively and locally,<sup>2</sup> it seems related to the economic necessities of the country only ultimately and indirectly. Its direct connection is with the provision of employment for all.

Now this concept, if we have correctly interpreted it, of once correcting all possible friction and then concentrating only on 'providing work' quite apparently holds great dangers to the type of economy we are considering. Even if the interpretation given by us to the 'accepted' meaning of the term full employment is

---

1. Page 21.

2. Page 20.



somewhat rigid, in practice, with the accepted full employment devices of budget deficiteering and spending to meet demand deficiency, the nature of the jobs created can be far different from what the economy may need. Our disagreement is not with the modern notions of full employment, but with the practical aspects and the context in which the concept is allowed to enter. The relative futility, from the point of view of total production, as well as the adverse effects, of deficit spending, we have already seen. We have had occasion to observe that the employment policy for an agricultural country is really an industrial policy. Meanwhile, under the canopy of this concept of full employment and owing to a complacency on the type of jobs State policy is concerned in providing, a comforting conclusion can accompany the emergent state of 'employment for all', that, thereby, the standard of living of the population is also being permanently raised.

In other words, the idea is definitely put forward that 'employment for all' and 'standard of living for all'<sup>1</sup> can and may well conflict. If they do conflict, as they must in the foregoing circumstances, it is also by now clear that the choice has to be on the side of industrial policy and standard of living and not of stagnant economic activity, rising prices internally and adverse balances externally. The effects finally of the latter are relentless; the economy must simply get back to a Keynesian equilibrium, at a lower level.<sup>2</sup> The first question that will arise is what happens, then, to the much sanctified and generally accepted objective of full employment. To go step by step, full employment in the all too simple sense of 'employment for all' here and now, is incapable as we see of fulfilling its own purposes in any long-period and stable manner. It would follow that conditions providing facilities of employment for all must first exist. In other words, the national income must first be sufficiently great, the cake must be enough to go round; and the structural set-up has to be such as will respond to somewhat unproductive employment, *i.e.* mere additions to purchasing power. It is therefore clear that policy needs first to

---

1. For convenience we continue to use the phrase 'standard of living for all' in the subsequent pages too. What is meant is, of course, a given 'minimum' standard of living, for at the moment there is no limit to which the standard of living cannot rise—if only the means were available.

2. That the redistributive welfare policy, of employment for all, depletes sources of capital creation is, in a poor country, obvious enough; but the same complaint has been strongly made for advanced industrial countries as well.



be directed towards increased production resulting finally in increased national income. In the end, the policy of employment for all can be compatible with the terms full employment, economic development and standard of living. Full employment may still be left to mean employment for all, but employment at two, three or more removes.

Almost the sole and the motivating reason for a special study of full employment in agricultural countries is the complications introduced, in theory and policy, by this very indirectness which the situation dictates. For, the transition from the present stage to optimum development can be very long (it may extend over decades) and therefore in practice very important. It is only for a later stage in these countries, or in the different contexts of already advanced countries, that the point about a standard of living for all could be assumed in the use of the phrase 'employment for all'. For, this assumption must first be real and justified or, if it is not, it must be added to the definition of full employment and afforded prior consideration in policy. It is the only manner in which the term can, finally, seek realisation of all its truer contents. Therefore, for agricultural countries, full employment means standard of living for all.

In this, the term standard of living for all is distinguished from the term standard of living. The former is the only one relevant to the objective of full employment. Mere economic development, connoting a prosperous national income, is of little relevance to the term full employment. In deciding on an economic policy, as we have seen and shall see later, economic development is the first step. But the term full employment is here studied as being ultimately a social desideratum of highest value, transcending just economic value alone. The phrase standard of living can mean only average standard of living. It is more a statistical abstraction, standing only in mathematical and not social relation to economic development and national income. The average so derived has often no counterpart in reality. The imperative call for structural and economic development should in the end, not be sacrificed either to the Devil of an Abstract Average standard of living or to the Deep waters of employment for all. The individual standard of living is the ultimate aim and *raison d'être* of economic policy;



and policy should *ultimately* subserve that end. Immediate policy, however, will be concentrated on creating the required economic context for realising the aims, through redistributed purchasing power and cumulative development of standard of living for all.

There is one point, yet to be noted. Idleness, it is said, "is not the same as Want, but a separate evil, which men do not escape by having an income. They must also have the chance of rendering useful service and of feeling that they are doing so."<sup>1</sup> This would veto any policy of 'employment for all', implying and built on schemes of payment for 'digging holes' and on Social Assistance, (though not strictly Social Insurance). To that extent, it creates no problem for an agricultural country that sees, as its first aim, a development programme. This of course does not permit a concentration of public works policies which *are* socially desirable, and represent an addition to created wealth.

For, balanced structural and economic development is the major economic policy, and the objective of 'full employment', wherever helped by special economic activity, must be subordinate to the priorities of the economic programme. This is not a new statement—it has been stated in preceding pages. What is brought out here is that State policy may have, for some time, to reconcile itself to a position that abjures social services and public works on any considerable dimensions and at the same time, faces, for a period, relative idleness or under employment in certain sections of the economy. This necessity is, of course, born of the concept that the standard of living for all is to be achieved by distributing from increasing and stable national income, and not by short circuiting the process.

The word 'distribute' here does not mean removal of Want without removal of idleness. Every economic activity in a development programme, is ultimately a purveyor of productive employment. Several items of work in a planned programme would take on the Social functions of a public works policy, if the State wishes to have it so—on this more will be said in Chapter II. Nor need only idle occupations be available at a later stage in development. Not even the richest country in the world has met the wants of

---

1. Page 20.



citizens so completely as to be unable to provide socially useful work. Public works is only a convenient omnibus term. Roads, houses, modern conveniences (so innumerable) are themselves enough to keep any State occupied with socially useful tasks.

The distinction between distribution and development obtained its due respect even in the heyday of commercial industrialism. In the words of Alfred Marshall,<sup>1</sup> "Many Social reformers in their desire to improve distribution are reckless as to the effects of their schemes on the production of wealth. They argue that if the distribution of wealth were somewhat improved the present or even rather a small national income would suffice for all the reasonable needs of man. But statistics prove this is not the case." Of late, this point has entered increasingly into the economic theorising on advanced countries as well. In the words of Lord Brand<sup>2</sup> "redistribution of income by taxation has now been carried to the limit and, I think, beyond it, if our main aim is to be the production of still greater wealth. For instance if it were to be decreed that no man in the country should have an income of more than £550 net of tax a year and the resulting surplus were distributed, and even if production were to remain as large as before, the addition to all other incomes would be quite small, some £25 to £30 a year. But, of course, if any such wholesale redistribution as this were to be made forcibly, production at any rate by private enterprise would be altogether undermined." More recently the following similar question was posed:<sup>3</sup> "The real issue before the country is not one of the structures and organisations through which the Government shall act but of the basic objectives of its policy. For a generation or so Britain has been moving away from the old acquisitive, economic society towards the welfare State. This change can be seen in a number of ways. It can be seen in the great growth of social security, not merely in the enactment of even more costly schemes of endowment for the individual but in the growth of the belief in all parties that the object of industry is not to create wealth but to provide jobs, that the aim of public policy should not be efficiency for the community, but security and protection for the individual. It can be seen in the enormous growth of the influence

---

1. Quotation Economic Journal, September, 1948, Page 319

2. *ibid*

3. Economist, November 27th, 1948, Page 868



of the State—not perhaps until the last three years—in State ownership, but in State control and State financing (before the first War barely 10% of the national income passed through the hands of the central and local Governments; now it is 40%), it can be seen in the steady neglect of capital creation—both of the thrift that creates savings and of the enterprise that uses them—and in the progressive engrossment of ever larger proportions of the national income in one form or another of current consumption. These ideas have captured all parties in the last generation."

In a sense, all that is pleaded by us is that before the programme of disbursement for provision of jobs for all is launched, the priorities for the economy have to be correctly arranged. We may also emphasise that our target does not controvert the under-consumption idea. The need for active supervision over total national consumption expenditure remains. But such supervision involves careful control and direction. In non-monetary terms, it would amount to an insistence that the overall planning must be wide in scope and must penetrate into the lines of economic activity proposed. Incidentally, however, an important point may at the same time be tentatively made. The idea of 'jobs for all' is put to the background only in deciding the fields for investment and disbursement. Within those fields, it may be said that the policy of labour 'intensive' which is likely to be largely adopted may be accepted as an encouragement to the principle of 'jobs for all' as opposed to the strict conceptions of the standard of living for all idea.

The standard of living idea includes the 'employment for all' result; only, it gives priority to the task of capital creation. In both these contexts, it is the twist given to national income disbursement that is important. It may be noted, therefore, that a Development Programme with 'standard of living' as the target, will be broadly the recommended policy as well as the interpretation given to the term Full Employment in our Title.



## CHAPTER SIX

# The Case for Development

THE case for development is already implicit in the pages of part one of this book. In this chapter, it is proposed, to examine some of the important ways in which the deficiencies in integration and diversification are manifested. Further, the implications for the external world are considered.

### (i)

The peculiar susceptibilities of the agricultural countries have been demonstrated. We have also seen, in a general way, the operation of certain factors leading to a low level of subsistence in some of these countries. In so far as the ends of a development programme are the satisfactions of social security, education, health, higher standards of living, ampler amenities, greater leisure, and higher cultural attainments, the poverty of means is patently a handicap. The richer agricultural countries could, certainly, organise most of the social service schemes, financially speaking. But they, too, would not escape the wide oscillations of national and individual incomes and would not be in a position to initiate economic action within, for sure recovery. The case is, however, more clearly brought out in a poorer country. Let us take a typical agricultural country, like Ceylon.

In Ceylon, it has been estimated<sup>1</sup> that "a family consisting of a husband, wife and two children would require for its minimum subsistence, on 1938 prices, Rs. 1.968 per day, or about Rs. 720 per annum. Its share of the national income, if it could receive it, would be Rs. 400. Whatever errors there may be in the calculations due to inadequate statistics, it is clear enough that the State cannot guarantee that every person in the Island will be maintained at the level of bare subsistence. Nor do we know whether the national income will rise or fall."

"We must not be taken to assert, however, that the country can afford the Social Services now or will be able to afford them in the

---

1. Report on Social Services, Pages 14-15.



future. Those questions can be answered from time to time by those in charge of the national finances."

"The great mass of the population, those engaged in agricultural occupations and their dependants, who together make up some 70 per cent of the population, have no surplus available for redistribution. The Economic Surveys of sample villages in the wet zone display a very low standard of life. They show that before the war most of the families in the selected villages had gross incomes of less than Rs. 20 a month, while very few had incomes of more than Rs. 50 a month. There is no doubt that similar surveys in the dry zone would show an even lower standard of life. This section of the population too, like the poorest-paid workers in the towns and on the estates, already pays comparatively highly towards the public revenue. As in all countries which rely heavily on indirect taxation, the lowest incomes carry a proportionately higher share of the national revenue, though the actual amount is very small. It is therefore clear that so far as social services are concerned the villages will be liabilities rather than assets. This is a special feature which differentiates Ceylon from countries like Great Britain, the United States, Canada, Australia and New Zealand. They have a high standard of life which enables the great mass of the people to contribute towards social services.

"The employed help to maintain the unemployed; the healthy help to maintain the sick; the adults not only help to maintain their own children and aged but also those who have no fathers or sons. In these countries social services are provided by the majority for the minority. In Ceylon, on the other hand, the standard of life of the majority is too low to enable it to contribute. Such social services as there are must in fact be provided by the minority for the majority. It would be useless (for the Commission) to recommend the redistribution of an income which is already too low. In the West the worker can help to maintain his fellows: here he has difficulty in maintaining himself and his family. Until the national income has been raised, we should be chary of Western precedents." It is the same tale in respect of several other desired schemes like education and housing.



These must be read with the connected point that the control of disease and famine and the supplying of social needs, in themselves highly desirable, reduce death rates and increase the size of population. There is no virgin territory for expansion, as there was for Europe in the 19th century. There is no greater danger, and no better indication of the urgency to expand, than such stagnation in economic conditions. Assuming, rightly, that the population originally lived at subsistence level, savings needed to finance industrialisation will get mopped up. It is an initial capital investment programme, worked through a development plan, that can ensure for the country a future normal and healthy rate of capital accumulation. There are also other factors that perpetuate under-development. Countries today cannot industrialise on long hours of work and starvation wages. At the same time, to maintain the subsistence wages, they need development. A further handicap is the absence of 'free' markets to sell in. Finally, there is little or no pre-industrial capital similar to that which Western countries had on the eve of their industrialisation—partly because "competition from machine made products prevented the formation of capital from pre-industrial manufacturing".<sup>1</sup> In line with our analysis of full employment theory, the benefits of investment by the Metropolitan countries really went to the latter. This investment further prevented that revolution in "education, skill, way of life, inventiveness, habits, store of technology, creation of new demands, etc", which are said to be more important even than the immediate product of an industry.<sup>2</sup> Finally, it resulted, historically, in adverse terms of trade for under-developed countries; the industrialised countries got the benefits of both rising profits from manufactured exports and lower prices for raw material imports.<sup>3</sup>

The logic of events has manifested itself as clearly as the circumstances would permit. That these manifestations have not emerged in the past as a fully fledged 'industrial revolution' has been due to

---

1. American Economic Review, May 1951, page 271. H. G. Aubrey, Role of the State in Economic Development.

2. American Economic Review May 1950, page 476. H. W. Singer, The Distribution of Gains Between Investing and Borrowing Countries.

3. Ibid, page 478. The nature of the capital investment affected the particular orientation given to economic development. Railways served practically only the 'plantation' areas, and no adequate provision of transport existed in other sectors, either within or in coastal trading. This must have obstructed the working of any influences that could provide the organisational set-up for the creation



the circumstances. There was a general helplessness in the situation and free forces were unable to work the change, especially in the light of the early lead by the advanced countries.

A practical resume of the need for development would be as follows.<sup>1</sup> "The progressive transfer of working population from agriculture to industry and services has been going on for a long time. This process is in line with certain basic economic trends. As technical advance raises incomes beyond a certain minimum, the proportion spent on food falls; the share of agriculture in total output is, therefore, bound to decline. Moreover, with increasing efficiency in agriculture fewer hands are needed to produce a given output. Rural income levels can in these conditions only be maintained or raised in step with industrial incomes if the proportion of the population which is engaged in agriculture is reduced.

---

of other agriculture, or preservation of small industry, not to speak of gradual industrialisation. c.f. c.g. Hubbard in *Eastern Industrialisation and its Effects on the West*: "India's position with regard to foreign capital is very different from that of Japan. Japan borrowed abroad to finance her industrial development but retained control of capital in her own hands and eventually evolved from a debtor to a creditor nation...But India...has suffered from the limitation that her use of imported capital has carried with it outside control over the choice of investments and hence over the general trend of economic development." There are again the cases of some African areas—c.f. Rita Hinden, 'Plan for Africa' "The gist of the situation (in the Gold Coast) is that the five main exports of natural resources other than cocoa, have been reduced to about one-quarter of their value in thirty to forty years..." With a total import trade of £8,000,000 annually, between £1,000,000 and £2,000,000 are expended in bringing foodstuffs from abroad. Among the items are canned fish and meat, flour and rice, biscuits, dried milk, edible oils, and slaughter animals. Timber is exported and furniture and building materials imported. The palm-oil industry has declined but edible oils are imported. "The very ability of the country to use the proceeds of the cocoa trade for buying attractive foodstuffs from abroad has diminished interest in home production, and it is only in years of lean cocoa return that a certain uneasiness about the weakness of the home food supplies is stirred."

An implication of the capital investments were debt charges. In the African areas, referred to, the charges varying from 5% of the country's exports and less than 18% of its revenue to 9% of the exports and 30% of the country's revenue, seem to "have been incurred almost solely for the purpose of providing transport for the export trade." "In the depression years, when the prices of raw materials were at their nadir, as much as one half of the exports of some countries was needed to pay off their debt charges; and in some colonies these charges were equal to a full third of the whole revenue of the country." c.f. also Lewis on Jamaica (*Agenda* November, 1944) where Banks and Insurance companies, the two principal financial institutions, are mentioned as "heavy exporters of savings".

1. Mandelbaum: *Industrialisation of Backward Areas*, Page 1.



It is a firmly established generalisation that for every great region of the world living standards tend to be the higher, the smaller the relative importance of agriculture as a field of employment".<sup>1</sup> "Measured by economic standards, the shift away from the land has not yet gone far enough. For there is still a large discrepancy between per capita incomes earned in industry and agriculture, if we take the world as a whole. As long as this consideration prevails, there is an economic case for occupational adjustment. The discrepancy exists mainly because there are vast and densely crowded areas, as in China, India and Eastern Europe, where almost the whole active population has remained in agriculture, although the land offers competitive and remunerative work only to part of this labour force. Industrial progress has bypassed these territories which between them contain over half the world's population."<sup>2</sup> For Eastern and South Eastern Europe, which includes Poland, Hungary, Bulgaria, Rumania, Yugoslavia and Greece, it has been estimated, on calculations based on a comparison between existing and optimum population density on land, "that of a total active farm population in South East Europe of rather less than 30 millions, between 6 and 8 million active workers are superfluous and could be taken off the land without loss to agriculture. In the course of the next generation, the area faces the prospect of a further increase by over 30% in the number of people of working age who will add to the already heavy pressure on limited agricultural resources unless other opportunities can be found for their employment."<sup>3</sup> Further rationalisation of agriculture is itself conditioned in these areas by industrial advance. "The growth of industry in excess of the natural increase in population by drawing surplus people from the land, would automatically raise agricultural output per head even

1. "Rich agricultural countries such as New Zealand, Australia or the Argentine are no exception. The ratio of farm to total working population in these countries is far below the world average (which is probably around 60%) and is steadily decreasing because of the expansion in service employment and also in manufacturing." This is often overlooked in superficial writing on economics. There is e.g. the following passage from Sir Ivor Jennings' *Economic Survey of Ceylon* (page 100). "If a Denmark could be produced in Ceylon, the case against industrialisation would be unanswerable."

It is unfortunate that in most respects—the views on free trade, on industrialisation and high-cost industry, and chronic unemployment and under-employment—the book is unfortunately misleading and would be a typical example, in the words of W. A. Lewis, of economics in its process of earning 'disrepute with laymen of ordinary intelligence.'

2. Mandelbaum: *Industrialisation of Backward Areas*, Page 1.
3. Mandelbaum: *Industrialisation of Backward Areas*, Page 2.



in the absence of changes in land tenure in crops and in farming methods. It would provide the means for supplying agriculture with more power, better transport facilities, marketing, and similar services; and by increasing the number of income-earners and hence the demand for (more valuable) food, it would stimulate agriculture and more specifically mixed farming which in South East Europe seems the most economical use of the land. The experience of those more advanced countries which in the earlier periods of their development faced similar problems of poverty illustrates the process by which agriculture is rationalised at the same time that an expanding industrial system absorbs parts of the rural labour force."<sup>1</sup>

It has been, therefore, quite logically asserted that "there is no reason why poor countries should accept as a dictum specialisation among regions which since it is based on existing cost relationships is rational only in regard to given conditions of under-employment." Like the infant industry argument, the infant economy argument is, in an important sense, true. It is reasonable, then, to recognise not only the trend among agricultural countries to industrialise, but also the intervention, by a planned programme, to enable the countries to get over their special difficulties. W. A. Lewis, writing on 'An Economic Plan for Jamaica', states that it is a commonplace of the history of economic development that in an unindustrialised country industrial costs are always high. Costs fall only as the country becomes industrialised, through economies, not merely of trained skill and discipline, but of sale. "It follows that if one is trying to estimate whether secondary industry will pay in a country not yet industrialised it is foolish to do so in terms of current costs". It is also rightly pointed out that the existing exchange rate is not necessarily the appropriate rate and could not always be taken for granted. Referring to a recent Government Report on the subject he adds "It applies static economic theory to an essentially dynamic

---

1. "One great advantage of mixed farming would be the reduction in seasonal unemployment in agriculture which is very marked in South East Europe. The quantity of labour which can be used throughout the year is much larger in mixed farming than in grain production. The change from the one to the other which would occur in conditions of industrial expansion seems a more effective way, in the long run, of combating a large-scale seasonal unemployment than attempts at providing work supplementary to agriculture in the winter period." The point is relevant to the structural framework, we attempt in Chapter 10.



problem. It takes an international price theory which applies only when the balance of payments is in equilibrium and applies it to a situation where the balance is heavily in disequilibrium. It takes a theory of cost which applies only in full employment, and uses it in a situation of marked unemployment."<sup>1</sup>

## ( ii )

We may set down certain factual information that has a relation to all this. "In the U.S. manufacturing production increased approximately 15 times between 1870-1938, while the number of wage-earners rose only 4 to 5 times and that of man-hours only two to three times. The output per man-hour over the period may have risen as much as six times as the use of mechanical power and labour saving machinery was increased."<sup>2</sup> Now, "If we assume that India's population and manufacturing were to continue to increase at the same average rates as (it did between 1896 and 1938) ) it would take some ninety years before the manufacturing per head would reach the figure of Japan in 1936-38 (which was still only 1/5 of that of the U.S.). Meanwhile the population, which is already extremely dense, would have increased by 4/5. Obviously a much more rapid development of manufacturing is required."<sup>3</sup> "It may be said with some justification that when in densely populated countries industry, transport, commerce and similar professions absorb more than the whole increase in population (thus reducing the number of people dependent on agriculture), the industrialisation process is well under way, but that when this is not the case and the pressure on the land increases the process is in its early stages with the outcome still in doubt."<sup>4</sup>

The following tables and graph,<sup>5</sup> which speak for themselves, will serve as useful reinforcements of these points.

---

1. Agenda, November 1944. The author continues—"This is the sort of thing that brings economics into disrepute with laymen of ordinary intelligence." c. f. also Singer in American Economic Review, May 1950—loc. cit.

2. League of Nations "Industrialisation and Foreign Trade." Page 48.

3. Page 58.

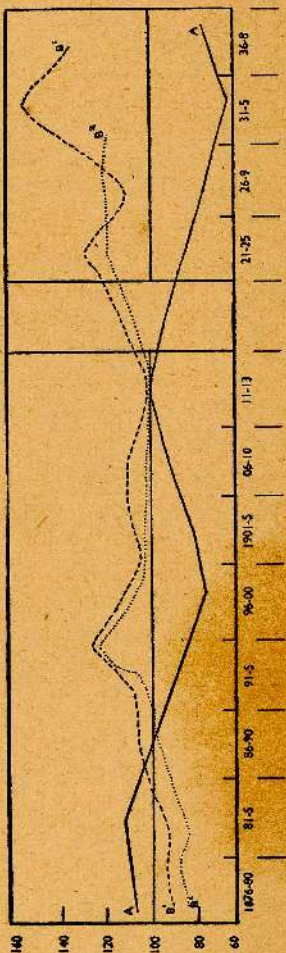
4. Page 64.

5. Pages 18, 65, 24-5 and 26-7.



## RELATIVE PRICE MOVEMENT AND TRADE

- A Quantum index for World Trade in manufactured goods as percentage of that in primary goods.
- B1 Price index for manufactured goods as percentage of that for primary goods.
- B2 Ditto, using the arithmetic average of the British import prices indices for foodstuffs and raw materials as representative of primary goods (entered as a check on B1 up to 1926-29).





## CHANGES IN GAINFULLY OCCUPIED POPULATION

Increase (+) or decrease (—) in gainfully occupied population (000's). Percentage share of total increase absorbed by:

Country	Period (1)	In Agriculture			Total			Other occupations (6)	Total (7)
		(2)	(3)	(4)	(5)	(6)	(7)		
Estonia	1920—1934	+36	+4	+40	90	10	100		
Mexico	1921—1930	+143	+25	+168	85	15	100		
Bulgaria	1920—1934	+602	+231	+833	72	28	100		
Greece	1920—1928	+550	+329	+879	63	37	100		
India	1921—1931	+2,500	+2,000	+4,500	55	45	100		
Latvia	1928—1935	+35	+30	+65	54	46	100		
Yugoslavia	1921—1931	+259	+320	+579	45	55	100		
Finland	1920—1930	+75	+168	+243	31	69	100		
New Zealand	1921—1936	+36	+99	+135	27	73	100		
Chile	1920—1930	+13	+97	+110	12	88	100		
Australia	1921—1933	+57	+493	+550	10	90	100		
Poland	1921—1931	-518	+2,001	+1,483	-35	135	100		
Hungary	1920—1930	-96	+272	+176	-55	155	100		
Norway	1920—1930	-58	+155	+97	-60	160	100		
Ireland	1926—1936	-30	+67	+37	-81	181	100		



**AVERAGE PER CAPITA EXPENDITURE IN PEIPING (China) AT DIFFERENT  
INCOME LEVELS IN 1931**

	60—	120	180—	240	360—	420	600—	720	1,200—	1,500	2,100—	2,400
Range of Family Income, Chinese \$	60—	120	180—	240	360—	420	600—	720	1,200—	1,500	2,100—	2,400
Average income per Family, Chinese \$	104		215		387		642		1,372		2,228	
Average income per person, Chinese \$	34.7		52.3		92.2		173.6		268.9		420.4	
Average expenditure per person in Chinese \$ for												
Food	21.1		31.1		45.6		63.4		85.9		93.8	
Manufactured goods other than food	1.4		3.2		11.5		25.5		59.0		96.2	
Other expenditure	10.1		14.1		22.3		58.4		101.7		168.2	
Total expenditure	32.6		48.6		79.4		147.3		246.6		358.2	
Average savings per person	2.1		3.7		12.8		26.3		22.3		62.2	
Percentage distribution of expenditure:												
Food	65		64		57		43		35		26	
Manufactured goods other than food	4		7		15		17		24		27	
Other expenditure	31		29		28		40		41		47	
Total	100		100		100		100		100		100	
Expenditure expressed as a percentage:												
Food	100		148		216		300		407		445	
Manufactured goods other than food	100		229		821		1,821		4,214		6,871	
Other expenditure	100		140		221		579		1,007		1,665	
Total	100		149		244		452		756		1,099	



## AVERAGE PER CAPITA EXPENDITURE IN THE UNITED STATES AT DIFFERENT INCOME LEVELS IN 1935-36

	500	1,000—1,250	1,500—1,750	2,000—2,300	3,000—4,000
Range of family in \$.....	312	1,120	1,612	2,221	3,394
Average income per family in \$ .....	84	280	413	555	828
Average expenditure per person in \$ for:					
Food .....	54	109	135	156	189
Manufactured goods other than food .....	21	66	98	142	202
Other expenditure .....	49	107	154	199	277
Total Expenditure .....	124	282	387	496	668
Average savings (+) or borrowing, relief (-) per person .....	-40	-2	+26	+59	+160
Percentage distribution of expenditure:					
Food .....	44	38	35	31	28
Manufactured goods other than food .....	17	23	26	28	30
Other expenditure .....	39	39	39	41	42
	100	100	100	100	100
Expenditure expressed as a percentage of that in the lowest income group:					
Food .....	100	202	250	289	350
Manufactured goods other than food .....	100	314	467	676	962
Other expenditure .....	100	218	314	406	565
Total .....	100	227	321	400	539



## PERCENTAGE DISTRIBUTION OF THE GAINFULLY OCCUPIED POPULATION

Country	Year	Agri- culture Fishing	Mining	Manu- factur- ing, Handi- craft.	Com- merce and Trans- port.	Admini- stration Domes- tic Service, etc.
<b>1. Typical Industrial Countries</b>						
U. K.	1930	7	5	32	23	33
Belguim	1930	17	6	42	21	14
Netherlands	1930	21	2	36	23	18
Switzerland	1930	21	—	45	19	15
United States	1930	22	2	30	27	19
Czechoslovakia	1930	28	2	40	14	16
Germany	1933	29	4	36	19	12
Austria	1934	32	1	33	16	18
Sweden	1930	36	1	31	18	14
France	1931	36	2	32	17	13
Italy	1936	48	1	28	13	10
Japan	1930	50	1	19	20	10
<b>2. Other Industrial Countries</b>						
Australia	1933	20	2	30	24	24
New Zealand	1936	28	—	24	26	22
Argentine	1930	30	—	—	—	—
Canada	1931	31	2	25	23	19
Norway	1930	35	1	26	22	16
Denmark	1930	36	—	28	18	18
South Africa White Population	1936	26	4	23	30	17
Others	1921	75	6	5	2	12
<b>3. Less Industrial Countries</b>						
Chile	1930	38	6	22	16	18
Uruguay	1930	44	—	—	—	—
Ireland	1936	48	—	15	13	24
Cuba	1919	49	—	20	16	15
Portugal	1930	51	1	18	9	21
Palestine	1931	51	1	15	15	18
Hungary	1930	54	1	23	10	12
Greece	1928	54	—	16	12	18
Spain	1920	50	2	19	8	15
British Malaya	1930	56	—	—	—	—
Finland	1930	64	—	14	7	15
Poland	1931	65	1	16	8	10
Estonia	1934	66	—	15	7	12
Latvia	1935	67	—	15	8	10
U. S. S. R.	1930	67	—	—	—	—



## Percentage distribution of the gainfully occupied population

Country	Year	Agriculture Fishing	Mining	Manu- factur- ing, Handi- craft.	Com- merce and Trans- port.	Admini- stration Domes- tic Service etc.
---------	------	------------------------	--------	--	---	---

## 4. Countries lagging in Industrial Development

Egypt	...	1927	67	—	11	12	10
Mexico	...	1930	68	1	13	7	11
French Indo-China	...	1930	71	—	—	—	—
India	...	1931	72	—	11	7	10
Thailand	...	1930	72	—	—	—	—
Colombia	...	1930	72	—	—	—	—
Venezuela	...	1930	72	—	—	—	—
China	...	1930	70-75	—	—	—	—
Netherland Indies	...	1930	73	—	—	—	—
Peru	...	1930	74	—	—	—	—
Brazil	...	1930	75	—	—	—	—
Philippines	...	1930	76	—	—	—	—
Roumania	...	1930	78	—	7	5	10
Yugoslavia	...	1931	79	—	11	4	6
Lithuania	...	1923	80	—	6	3	11
Bulgaria	...	1934	80	—	8	4	8
Turkey	...	1935	82	—	8	4	6

(iii)

It is now necessary to study the relation of the agricultural country with the rest of the world, and its implications for both. It is clearly essential to substantiate the rationale of a development programme in this context. The structural set-up existing in each country would, from the moment of change, no longer represent any final position of mutual advantage. The new movement must needs have its reaction on the hitherto industrialised countries, where a readjustment is called for to meet the new situation. The question whether in the international sphere it pays agricultural countries to industrialise, and whether industrial countries will not lose by it needs to be answered. On the side of the agricultural countries, our theoretical study earlier should have the answer ready. We shall make the inferences warranted by it, therefore, in proceeding with the question raised here.

To take the industrial country first, the mistake is often made that industrialisation has as its consequence the stoppage of imports, as the industrialised country can produce everything for itself. For



example, Stamp stated:<sup>1</sup> "Loans assume a completely new aspect when one country by its financial operations is immediately equipping another country to be competitive with it in the world's markets and not merely complementary." We may straight away admit that this may be so if we consider the process of industrialisation as one which stops at a certain point. But it does not. What is meant is that, in the new dispensation, raw material and simple manufactured goods could be made by the newly industrialised countries, other products requiring a very high proportion of skilled workers could be manufactured by the older countries, and a planned exchange of products could be developed. The new structures in older countries will therefore specialise in high quality and 'precision' goods as well as complicated machinery and so on; while the "newer" economies will engage themselves only in simpler methods. The crucial factor will be human skill.

A good example is the case of the Dominions, prodigious producers of primary products. Their industrial growth at least up to World War I was closely linked with the growth of their foreign trade. Their importance as markets for the manufacturing industry of the 'older' countries may be roughly gauged by the facts that the net import of manufactures into the British Dominions in 1926-9 was about 50% larger than that into China and India with 30 times their population and that their net import of manufactures per capita was 40 to 50 times greater than that of the last mentioned two countries.<sup>2</sup>

Normally the continuation of imports of manufactured goods after the process of industrialisation has got under way, is likely to be encouraged by the ease in the balance of payments that usually accompanies the approach to industrial maturity and by the increased demand for goods resulting from higher incomes.<sup>3</sup>

The following chart generally supports these contentions.<sup>4</sup>

- 
1. Quoted by H. Frankel, *Economic Journal*, June-September, 1943.
  2. League of Nations, *Industrialisation and Foreign Trade*, Page 76.
  3. *ibid*, Page 78.
  4. *ibid*, Page 85.



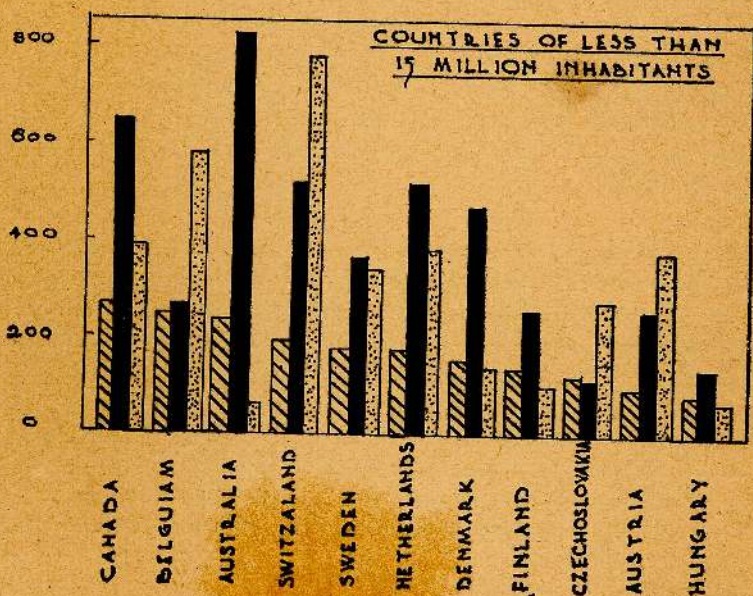
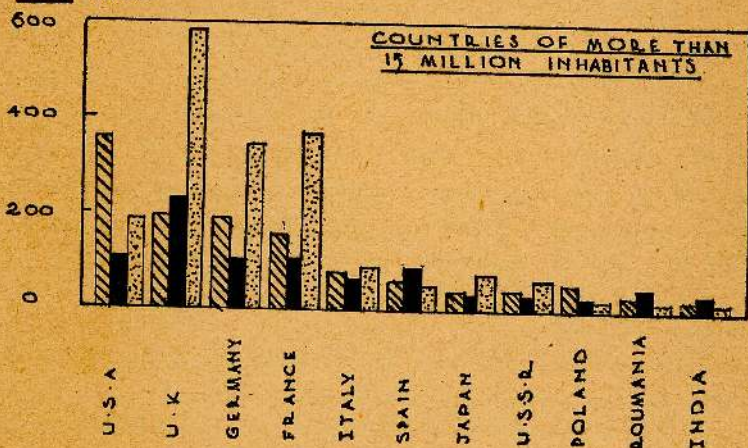
# MANUFACTURING AND TRADE IN MANUFACTURED ARTICLES PER HEAD OF POPULATION IN 1926-29



Manufacturing production (gross value excluding duplication in dollars) per head.

Imports of manufactured goods in tenths of dollars per head.

Exports of manufactured articles in tenths of dollars per head.





Let us consider this closer. It has been well stated that the demand for the articles which are produced in the first stages of industrialisation is usually relatively constant and inelastic. It frequently happens, therefore, that imports of such articles tend to be reduced as domestic production grows. When imports of manufactured articles increase notwithstanding this is due to a demand for other kinds of manufactured goods. This demand is a result of the increase in wealth that follows industrialisation ; it is diversified and oriented towards higher qualities of goods and usually varied according to taste and fashion. The domestic industry is naturally not ready to assume production of these goods ; moreover the variety of the products, and the narrow limits of the domestic turnover do not always permit of economic production in the country concerned. Another type of demand which naturally develops as industry expands and is usually met largely by imports is that for manufactured capital goods,<sup>1</sup> in particular machinery. Only countries with a considerable domestic market and highly developed industry can attempt to achieve a high degree of self-sufficiency in their supply of such goods.<sup>2</sup>

The best approach to the question is to see that in the new situation the old international division of labour based mainly on differences in natural resources will not hold. It is precisely the discovery of each country that it has the means with which to institute manufactures that has given birth to our problem. The

---

1. There is also a slightly varied angle on this which may be worth noting to avoid confusion with the argument above. Usually, countries with an undeveloped industry depend upon exports of primary products for financing imports of manufactures. Where such exports represents a considerable share of the production, there is a considerable market for industrial products.

"An economy permitting of a highly developed commercial exchange of this kind, however, seldom expands over big areas; it is naturally confined to regions with good communications to ocean ports. Islands, peninsulas, and coastal countries with a large agricultural surplus and too small a market to afford a basis for a diversified industry thus present the best example of a developed exchange of primary products against manufactured goods."

Of the following countries in this category, each with a very small manufacturing production per head (except to the extent that it consisted of processing for export), British Malaya, Cuba and Chile recorded in 1926-29 a per capita import of manufactured articles of about the same magnitude as highly industrial countries of a similar population (as recorded in the following table) (Industrialisation and Foreign Trade, Page 86).

2. Page 98.



result will not however be *no* international division of labour and no international trade. On the other hand, a new fact emerges from a closer scrutiny and that is the significant possibilities of an international division of labour 'based mainly on differences in human skill'.

Now, from the point of view of an advanced industrialised country like Britain, for instance, we should think that certain very definite advantages accrue from this change and that the older arrangement, at least after the nineties of the last century, only put her at a disadvantage relatively to certain other countries. In the case of the 'raw material' producing countries, the purchasing power being necessarily low, 'quality' goods would not find a ready market. It is said that Britain improved her cotton industry considerably in the course of the 19th century and began to produce goods of higher quality to be sold mainly in Britain and other countries, which, in the course of their industrialisation, had created classes with a high standard of living similar to the British. On the other hand, the newly industrialised countries, first Germany and then Japan, began to specialise in cheap goods suitable for the mass of their populations and the backward countries producing raw materials. German export of cotton goods in the nineties consisted almost entirely of cheap products, whereas only 1/3 of British exports consisted of lower quality goods. A.W. Flux said in 1897, in an article on German competition, that 'Our trade outside the British Empire shows extremely satisfactory expansion, but our exports to our colonies appear to be dwindling'. The standard of living of the colonial countries did not rise enough to render convincing the argument of the English merchant who said 'this is the best article of its kind ; take it or leave it, but it is the cheapest in the long run.'

---

		Population 1926-29 (000,000's)		Imports of manufactur- ed articles, \$ per head (annual average 1926-29)
British Malaya	...	4.0	...	41
Cuba	...	3.6	...	31
Chile	...	4.1	...	28
Ceylon	...	5.4	...	8.9
Philippines	...	12.0	...	7.3

There is a strong contrast between these countries and India and China, which export a minor portion of their primary production. "India's annual import of manufactured goods in 1926-29 was only \$2 per head; China's \$0.9."



The success of Japan's competition against Britain, Germany and other advanced countries had the same roots as the previous competition of Germany against Britain. Mr. Barnard Ellinger attributes the Japanese success not to the difference in labour costs but to the fact that 'Japan understood how to satisfy the world's demand for cheap bulk cloth by using a type of raw material which although not as good as what we use, is sufficiently good to satisfy the world's requirements.' Mr. G. E. Hubbard endorses this opinion concluding that 'in the past Japan's greater concentration upon low quality cotton made from cheap raw material has been no small part of the cause of her success in winning British markets.' We may say in other words that Japan's success was greatly due to the low-purchasing power of the population in the European colonies and semi-colonies. It is interesting to note in this connection that it was precisely during the crisis of 1929-32 with particularly affected the countries producing raw materials and food stuffs that Japanese exports gained their momentum.<sup>1</sup> The following, for instance, illustrates that :—

	Dominican Republic		Haiti		Honduras	
	1929	1935	1929	1935	1929	1935
Percentage share of Japan in total value .....	0.4	11.8	0.1	17.7	0.5	10.6
Percentage share of cotton piece goods in import value	10.2	13.7	14.4	22.7	16.2	15.2
Cotton piece goods imported in tons (000's) .....	18.3	20.0	2.1	2.8	1.7	2.0

"When in spite of the ravages of the depression in the early 1930's, certain undeveloped countries not only maintained but increased the quantity of the textile products they imported at the same time as they shifted over to Japan as a supplier, there is

1. Frankel, *Economic Journal*, June-September, 1943, on the last two paragraphs.



reason to assume that the low prices rendered factory-made textiles available to layers of population which had previously not had access to them."<sup>1</sup>

Naturally, the opportunity of thus opening up new markets through a reduction in prices does not always present itself. The demand for the article the price of which is reduced may be inelastic in the importing country. While the supplier which lowers its prices will gain at the expense of its competitors, the total quantity will then remain at its previous level. But this is not the end of the matter, for as the import value of the article considered declines, there is likely to be a corresponding rise in the amount available for the import of other goods. The new demand thus exercised may at least to some extent benefit those industrial countries which suffered losses in their sale of the article first considered.<sup>2</sup> It must be remembered, however, that this benefit to older countries cannot be so great as that from the higher demands created by industrialisation in the agricultural countries.<sup>3</sup>

"To sum up, there is nothing to indicate that older industrial countries are bound to suffer from competition with younger countries." The only way to create a market in backward countries for the better goods is by increasing their purchasing power. That is possible only by increased industrial activity. The advanced countries, instead of losing, will then no longer meet with an impasse; and the backward countries will in turn get the benefit of a more prosperous economy.

The same opinion would appear to have been held by another student of the subject. "Generally speaking one should expect that the relative importance of international trade—that is the proportion of economic activity carried on for exports or dependent on imports—will decline as the result of industrial advance. This follows partly from the growing importance of services of which many have to be performed locally. Also as the range widens of things which can be produced, perhaps at little more than the import

---

1. Page 113. Industrialisation and Foreign Trade.

2. Page 114. On this paragraph.

3. The difficulties of old industrial countries, in competition with the 'new' industrial countries that sell cheap, are worsened without multilateralism, for several 'new' industrial countries would pay with their own manufactures for import of primary products. "While in 1928, for instance, there had been an



price, in a certain area, the scope for useful specialisation becomes narrower. But of course the absolute volume of international trade may expand. Historical experience in fact strongly suggests that wherever industrialisation leads to a significant rise in the national income, the demand for imports will also rise, although in the long run, not in the same proportion."<sup>1</sup> (While on this subject, a related point has been raised by the same author. "There can hardly be serious disagreement that substantial readjustment in the mature countries cannot safely be carried through under *laissez-faire* conditions";<sup>2</sup> an even truer point would be the ineffectiveness of *laissez-faire* conditions in the agricultural countries. We shall discuss this at some length in a later chapter).

So far, we have only vaguely shown that the transition is of advantage to the agricultural countries. Unless we give greater substance to this side, the argument that the Structural Problem is real, necessary or inevitable for the older countries themselves is not likely to remain indefeasible. For why not 'agriculturalise' and further increase purchasing power; why industrialise and disorganise the 'status quo' which compared to the 'transition' stage at least, promises the graceful 'economics' of large scale production and hereditary specialisation.

It is demonstrable,<sup>3</sup> from this angle as well, that the change is not only advantageous but vitally necessary. The argument is already implicit in Part I of the Book; we may lay it out here in the required order.

International trade with a division of labour based mainly on differences in natural resources has today serious consequences for any agricultural economy, be it Australia, South America, India or China. Theory leads us to the conclusion, which experience has substantiated, that the dependence of an economy for its income on

---

aggregate export surplus of £78 million in British trade with Australia, Brazil, British Malaya, Ceylon, China, India (with Burma), and the Netherlands Indies, trade with the same countries ten years later resulted in an import balance of £52 million; the share of these countries in British exports fell simultaneously from 28 to 22%. (Industrialisation and Foreign Trade, Page 115).

1. Mandelbaum, Page 16.

2. Page 18.

3. The paragraphs following are substantially taken over from my 'Ceylon, Beveridge and Bretton Woods', Pages 21-3.



one or two major industries (especially if they be agricultural) will bring with it an element of extreme instability from season to season that might gravely curtail income and imports of necessaries. It will entail the inevitable repercussions of crises and unemployment within the country. Dependence abroad for most of the necessaries (in Ceylon that includes rice as well) will seriously affect the 'terms' on which these countries can trade with others for imports in return for their exports. The demand for the exports of the agricultural countries will be relatively inelastic. No countervailing advantage will be present, since the demand for their imports of foreign goods will themselves be inelastic. In recent years (*i.e.* pre-War) the supply of exported products of the agricultural countries has exceeded the demand.

The improvement in the 'terms' obtained by means of 'restriction' (assuming away even the difficulty that it may not be effective in organisation, and presently also the difficulty arising from synthetic production) has never been considerable enough to solve the problem, for the reasons mentioned about the demand for imports of foreign goods. Besides, the greatest objective, the abolition of unemployment came no nearer solution. A better alternative to "restriction" is elimination of the 'high cost firm' and employment of the labour thereby released, together with the others, in the exploitation of available industrial resources. Nor can these countries secure the required volume of imported 'necessaries' from abroad, by just producing 'more of their agricultural goods'.<sup>1</sup> An increased output may only mean a decreased total revenue now—again due to the peculiar conditions about elasticity of demand by industrial countries for exports of the agricultural countries. The result is in all probability, a dilemma. In brief, the industrial countries are equipped with a far greater bargaining power and just the reverse is the case for the agricultural countries.

In the end, whatever the measures adopted, the bane of a continual deficit in the balances will continue. It is futile to employ a modern 'employment policy' with budget deficiteering.

---

1. This is generally recognised by students of the subject *c.f.* Tse Chung Chang "It is conceivable that in a particular case a favourable change in the relative quantities may be completely offset by an unfavourable change in the terms of trade..." page 12, *Cyclical Movements in the Balance of Payments*. Lewis in *Principles of Economic Planning* demonstrates the same possibility in the case of an advanced country like England. *c.f.* page 68. Regarding his endorsement for backward countries *vide* his page 124.



The better part of the resultant stimulation to business activity (the 'multiplier' effect) which may be expected to increase employment and income, will 'leak out' to the foreign countries whence the imports of the 'necessaries' have been coming and affect the terms of trade further. (Incidentally, this futility is also shared, for slightly different reasons, by any country wherein foreign trade plays a large part. The criterion here is rather the extent of the 'diversification' of the economy and not merely its industrial or agricultural nature). A sound 'industrial' policy is essential to overcome these weaknesses.

The movement, therefore, towards 'industrialisation' seems, on a study of the implications, to be entirely in the right direction; and international trade with division of labour based mainly on differences in human skill is mutually beneficial. Increased prosperity within for agricultural countries, increased imports (on satisfactory terms), consequent higher demand for exports and further prosperity in international trade, are the results.

We may now proceed to a closer study of the steps necessary for such an employment policy.



## CHAPTER SEVEN

# The Field for Industrialisation

ANY act of investment is, in a sense, a proposed act of development or industrialisation. It would hardly be fair to the requirements of our analysis, however, to identify any aggregate of such acts with a programme of development, such as we envisaged previously. It is important, therefore, to decide what *type of investment* programme should be adopted. It is also necessary to be clear as to what is meant by industrialisation. We shall take up these points in turn.

(i)

In a context of indiscriminate investment, neither savings nor the best endeavour and will could assure the results that we look for. There would appear to be two points in regard to this. A utilisation of financial resources may not really be towards physical production. Secondly, whatever portion has been used for actual output of goods need not necessarily be on those that we would consciously select for investment. We shall see more, later, on the non-coincidence of conscious selection and selection based on normally conceived business or social considerations. Here we shall assume that there is an increase of production by the acts of investment; but that the investment is indiscriminate. Under these conditions, such a programme of 'development' is bound to come in conflict with the requirements of economic policy. Without ensuring diversification there is no field for industrialisation. So much is more or less already familiar ground.

What is to be investigated here is, what sort of diversification is essential. In an industrialised country like Great Britain, for instance, it would not be advantageous at all to seek to diversify by launching a programme of production in raw material and food supplies, just on the simple reason that these constitute an overwhelming proportion of her imports. The economy is highly integrated and diversified enough to secure a high standard of living. On the other hand, could the British analogy be adopted? Could we recommend a policy of integration by more specialisation



and extended range of production in the export and home industries of agricultural countries? In other words, we have to decide whether this diversification is to be (I) of export industries or (II) of a set of new industries replacing imports, or (III) of other (home) industries, e.g. house-building, furniture manufacturing and so on.

In regard to (I), we have seen already the inability to rectify the balance of payments and the economic problems caused by further expansion in the existing export industries. The process of diversification, however, involves the creation of industries other than those existing. The question then arises whether there is any scope either for 'processing' of present exports or development of other exports. Lack of natural skill, capital resources and the lag of decades behind the advanced countries for the moment definitely exclude such a diversification on any considerable proportions. It is true that there is considerable scope for further processing of several of the present exports. It can, also, be true that geographical resources will indicate large possibilities for such a future—though this varies from country to country. Ceylon for instance, is not too well favoured, while India and China have great potentialities in their mineral and industrial resources. But it is not at all likely that a hope of increasing 'means' merely by export will bear fruit. In a sense, it would seem ludicrous to presume that countries needing to import simple manufactures and even food, could compete immediately at world prices by export of manufactures. That is not to say that agricultural countries, even small countries, cannot have first rate export industries. Porcelain, handicrafts, glassware, tourism are all great possibilities. In fact, one thinks that tourism and handicrafts (the latter in so far as we fit it later in the scheme of rural development) should come high up in our priorities. There are also small countries having highly advanced export trades in watch-making and so on. They afford a sound indication that certain exports are not beyond the ability of agricultural countries; the same goes for industries in respect of large agricultural countries. In these however, 'quality' or 'uniqueness' is fundamental. Further, no assistance in cost of production will immediately establish a prosperous export industry, nor even a home market; it will be a misdirection of means to concentrate resources on such industries. That must come after the economy has attained stability and a certain standard.



The final supremacy of these industries may take a decade or a century to be established in the world. On balance, the immediate development programme should seek in this field only such items as tourism and handicrafts.

The problem of the balance of payments and that of low subsistence have therefore to be solved by operation in different fields. Diversification by setting up 'industries' to replace present imports should recommend itself as being eminently fitted. For one thing, the present imports are largely not needed as raw materials for any existing export industry nor other industries. For another, the inauguration of such industries could proceed without impinging on any of the factors relevant to the existing export industries. For, it is implicit in the term 'agricultural countries' that labour is in abundance and seeks employment. The reduction in imports thereby would help the import of capital goods and the like; the economy would acquire a diversified and integrated framework; and a fruitful utilisation of employment devices is made possible.

This is not saying, however, that a mere substitution of industries within, for certain important imports, would necessarily solve the problem of low subsistence. It is of course certain that it would raise the level to some extent. The extent, however, varies. The table already given in the previous chapter<sup>1</sup> would show that subsistence goods, at those values per head, certainly missed a vast population in India and China and a considerable portion even in the others.

To the extent that imports per head are small, therefore, the new programme has to seek not merely to replace them for home production of those quantities, but has to adopt a much heavier programme of production. It may also have to be a more varied one. Low subsistence can imply not only a minimal import of physical necessities, but also virtual non-importation of several 'psychological' necessities. It is, of course, possible to argue that in the economics of full employment an investment programme just enough to replace the selected imports should impart the requisite diversification and integration for 'private' effort and 'free forces' to do the rest and that further policy at the 'conscious' level could be confined to the employment devices. There is much in the

---

<sup>1</sup> P. 74 above.



point raised. The verification, however, cannot easily be deduced but has to be made empirically in accordance with the particular circumstances. We shall discuss this in the next chapter.

In any case, the internal investment adopted would mean a fairly wide acceptance of (III) above as well, as one of the fields of industrialisation. While accepting this, however, we have to be careful against certain dangers inherent in the concept. This particular field would, by definition, include all activities like house building, furniture making, construction of roads, and similar public works; it may include also several activities answering to the formula of "digging holes in the ground and filling them up". At an extreme position, it could therefore, amount to a direct policy of subsidising purchasing power and strengthening consumption demand.

On the other hand, the importance of houses and roads as a part of the full employment policy cannot be questioned. What has been pointed out is that a continuous and long term policy based on just these would certainly neither help full employment, nor economic stability.<sup>1</sup>

We may now be in a position to answer the question set out adequately. It is largely a question of establishing clear priorities in the national programme for each of these fields. But the dangers inherent are also great enough for us to be warned that these priorities must be clearly understood and steadfastly adhered to. It is our conclusion on the foregoing brief analysis that the field for industrialisation in agricultural countries is definitely based on (II) above and largely confined to it; to the extent that certain items in (III) become necessary to setting up of industries under (II), the development programme will cover a large range in this field as well. The actual extent depends on the particular circumstances of each case and each country. (III) is also important in the sense that further raising of living standards and employment level will depend on the additional investments in this category.

---

1. There was an element of truth when the Physiocrats considered agricultural produce alone as wealth. We could substitute, with truth, wage-goods industries, in the *Tableau Economique*. c.f. for some interesting comments Mary J. Bowman in *American Economic Review*, May, 1951, page 1 et seq. "The consumer in the History of Economic Doctrine." There are hints that the Physiocrats were not unaware of the multiplier process either!



But this belongs to a later period. As for (I)—in the context of the countries we are considering, the scope is very limited (confined chiefly to items like tourism, fruit canning etc.,) and, 'chronologically', less urgent, save in so far as certain cottage crafts become necessary to optimum working of the village unit. The general principle should be that attempts to solve the problem of the agricultural economy through this category are out of the question, that therefore, essays in this field could be made to wait and that investment therein attempted only wherever feasible under world competitive conditions.

(ii)

The term Industrialisation—We have generally used the terms Full Employment and Development in preference to the term Industrialisation. There has been no doubt, however, that this last term has an intimate relationship to the others. In so far as it is used in the context of agricultural countries, it is necessary to be aware of its exact significance. It is known, of course, that the Industrial Revolution lent prominence to the word. It was coloured by the striking phenomena of that era, and came to be inevitably associated with an overwhelming introduction of capital equipment. The larger the rate of such installation, the greater the industrialisation that was considered to take place. The significance of land and, especially, of labour, dwindled in relation to the managerial and capital units in production. There was a historical awareness of this in the 'philosophy' of Luddism that seized labour at a certain period; a philosophy which failed to become more decisive than it was, only because the industrial potential itself was enormous enough and its growth rapid enough, to swallow not merely the existing surplus but also the phenomenal increases in population that Europe experienced during that century. In this rich saga which has been romanticised so often, the eyes that were prepared to be enthused and impressed by the slower moving 18th century were very few indeed. But studies were not wanting to the effect that the Industrial Revolution really began in the 18th century or even earlier.

It has, in fact, been demonstrated that, in England, the beginnings of the Revolution were in the great reforms of the land tenure



system, in the consolidation of the holdings, in the realisation of a more scientific agriculture and animal husbandry, and in the great accumulations of commerce from the Mercantilist days down.<sup>1</sup> It was considered the more substantial part of the revolution in the sense of being the initial necessary aspect which made the more spectacular second half possible. Our purpose is not that of a historical enquiry, but the foregoing is important in relation to our agricultural countries.

Industrialisation is not necessarily characterised by heavy capital investment. Any situation where, the capital content vis-a-vis the existing combination is even slightly increased, is an act of industrialisation.

Heavy investment may or may not be in the interests of better combination of factors. In any level of industrialisation, there can be an overdoing of the process. This description may run counter to the oft repeated contention that industrialisation necessarily means higher incomes. This would appear to be associated with the generally true principle of increasing returns as always obtaining in industry. By a general historical custom, it is assumed that addition to capital automatically means a more economical association of the various factors of production. Hence the parallel statement, to put it crudely, that industrialisation is mere addition to capital and vice versa; and that both are indicated finally as higher incomes. A full employment policy worked out on the example of the industrial countries does not necessarily mean higher incomes; a situation is perfectly possible where it can mean less. Development means higher incomes and such development implies and means some increased capital content vis-a-vis the existing combination. But the term industrialisation in the popular sense, has to be received with some caution. We should rather uphold the relation of higher incomes to Development, than of Industrialisation (differently understood) to it.

---

1. c.f. Dobb, "Studies in the Development of Capitalism". The 'Mercantilist' merchants played their part in breaking down gild restrictions, but apparently they became themselves reactionary and it was left to country Merchant Manufacturers to carry on from where the movement was left. Land reforms and capitalistic farming, in addition to bettering agriculture, also created a rural proletariat and an internal market for the products of agriculture—so necessary for the revolutionary economic developments that followed.



For the principle of development is not just that addition of capital referred to, but the optimal combination of factors. Viewing the question from the point of view of capital, we may note that the degree of capital intensity, or the optimal amount of capital, varies in relation to the intensity of the presence of the other factors concerned. The principle of optimal combination gives various optima in respect of the degree of capital intensity according as conditions for various economies (and regions) are different, one from another. The degree of the scarcity experienced (conversely abundance) in respect of the various factors concerned—resources, labour, capital, skill (managerial, technical etc.)—would indicate varying types of combinations. Once the principle of optimal combination is recognised, it is evident that any degree of organisation below this level represents lower income. It is also equally clear that any degree of industrialisation that exceeds these optima assigned to the various factors cannot bring higher incomes. Economic development and full employment programmes then, we interpret in terms of this optimal combination—though as we shall see later, the term is not everywhere confined to a narrow business sense, but given justification in a much wider and more relevant field. The objective implies higher incomes. So long as we do not forget the foregoing points industrialisation can, for general convenience, be interpreted to mean higher income.

Industrialisation in the 19th century sense is not recommended unreservedly. A greater intensity, industry-wise, is necessary. Scientific rationalisation of the economy, with 'economic' allocation of factors is part of the process. The rationalisation of land tenure and the very act of diversification (irrespective of the additional incomes from the new economic activities) are part of the industrialisation. They can bring higher incomes themselves to the economy as a whole. Large scale programmes for agriculture and raw materials and certain 'processed' consumption goods would come within the term industrialisation. Blind manufacture-phobia of any and every sort is the other extreme from mere intensification of plantation and raw material economies.

It has been observed, by more than one student of the subject, that a fairly high correlation exists between low per capita incomes and a high percentage of the population engaged in agricultural



production. This is not the same, however, as saying that higher per capita incomes are related to the amount of capital investment in industry. New Zealand, Canada and Denmark whose investments are predominantly in agriculture have high per capita incomes. Of course, they had only 28%, 31% and 36%, respectively, of their gainfully employed population in agriculture. It means that a rationalisation and industrialisation of agriculture is as much a part of industrial development. This development represents one of the optimal combinations, referred to in the several theoretically possible.

There is also the argument that industrialisation, in the sense of capital investment, may not be the cause of higher incomes. A real or potential high per capita income may be the cause of the industrialisation. Resources, skill, natural and biological factors, social and agricultural organisation can, in varying degrees, determine productivity and income whether or not industrialisation takes place. "That this is the more probable causal relationship rather than a direct sequence from industrialisation to better standards of living seems to be emphasised by the very marked differences in incomes within the high income countries themselves. One would scarcely argue presumably that in the United States the low incomes in certain States was in any fundamental sense chargeable to the absence of industrialisation nor—what is even more important—that more industrialisation would certainly raise their per capita income."<sup>1</sup> It would be mistaken, therefore, to take all else as data and only industrial capital as the variable. It is to avoid misapprehension on such a count that we have chosen to identify full employment with development—and to use the term industrialisation in this field only in so far as it conforms to our interpretation of it! As has been well said, our "danger is especially great where industrialisation is used in a narrow sense of simply having more factories or industrial plants."<sup>2</sup>

Statistically<sup>3</sup> we may just say that a country is getting 'more industrialised' on the following basis, viz. that of increasing proportions of the working population in secondary and tertiary pro-

---

1. Buchanan, *Economic Journal*, December 1946, page 537.

2. Page 538.

3. Of course 'Statistical correlation does not necessarily demonstrate causal relationship.' *Economic Journal*, December 1946, Buchanan.



duction. "For convenience in international comparisons production may be defined as primary, secondary, and tertiary. Under the former we include agricultural and pastoral production, fishing, forestry and hunting.

Mining is more properly included with secondary production, covering manufacture, building construction and public works, gas and electricity supplies. Tertiary production is defined by a difference as consisting of all other economic activities the principals of which are distribution, transport, public administration, domestic service and other activities producing a non material output."<sup>1</sup>

We may conclude with this definition of Hilgerdt. "The industrialisation process is not confined to the establishment of a manufacturing industry, but involves a change in the whole economic structure of the country concerned. This change may be briefly characterised as implying an extended division of labour complemented by a system of distribution and exchange of goods functioning in a developed 'money economy'.<sup>2</sup>

---

1. Page 540, footnote 1.

2. Page 540, footnote 2.



## CHAPTER EIGHT

# The Machinery for Full Employment

**H**AVING defined full employment and in many ways clarified the content of full employment, we have so far left one very important aspect of development somewhat nebulous. It is the framework in which the work of development is to be implemented. We must decide the nature and the degree of State participation in development policy.

(i)

Agricultural countries are bound to encounter considerable difficulties during the launching of ambitious programmes. It is evident in several ways from the previous chapters that rank individualism is out of the question. Some direction in economic and financial matters is assumed. Is the State to provide basic needs like hydro-electricity, railways, etc.,<sup>1</sup> hoping for the rest to come by itself (as intended in the drafting of the pre-1947 Government of India Plan) ; or is it to be a Bombay Plan with the State controlling, in broad outlines, directions, trend, etc. as well ; or is it to be a 'Russian' (by which is *not* meant 'Communist') plan ? In short, between the principles of free enterprise on the one hand and complete planning on the other; at what point will we rest and find the ideal basis for development of the backward economy ?

We have already referred to a sense in which high incomes can be the cause of industrialisation and not vice-versa. In the typically agricultural countries, higher incomes are not data but desiderata. Further, in the typically agricultural countries several of the items like railways, roads, river development (especially on the T.V.A. model), airports, are highly capital-intensive in relation to income. This double factor, then, of small annual savings and almost an inversely heavy draft on them throws an 'initial major barrier' and, in the words of a writer, "for many low income countries, this ... has never been surmounted".<sup>1</sup>

---

1. Even within a restricted sphere there were certain characteristics that were notable. e.g. In the thirties in India the representative proportions of allocation in the Budget on Railways was something like 14% ; on agriculture and irrigation 1% & 3% respectively.

1. Buchanan, *ibid.*



As a result, especially where backed by the appropriate social philosophy, plans of developing for structures in transition have been put forward which would seem to have the appearance of being able to recommend themselves eminently. It is far from our purpose to deny that railways, roads, canals, hydro-electric power stations and other public utilities are highly essential, and more so where they are totally lacking and are a natural obstacle to economic progress. What is denied are the two vital points that may be inferred therefrom, namely that the problems created by the financial disbursements on such projects are insignificant or harmless ; and secondly, that in the course of their giving rise to new investment opportunities they will also actually lead to the investment envisaged. On the first, as we have seen in the last chapter, the proposed plan is only too likely to increase the volume of imports of necessaries ; and to quote ourselves from a previous chapter, 'the multiplier effect will work predominantly to the foreign advantage and national disadvantage. On the other hand, the industries on which the new demand is to operate must be simultaneously existing or created.' In the absence of this, the proposal presumes that the other aspects of development follow almost simultaneously. They are expected to be effected not through public but private enterprise. This involves the second point raised above. "Even if the probable adverse multiplier effect can be minimised there is the point that must first itself be apparent, that investment in such enterprise will lead to a clearly assignable and desirable increase in employment and incomes only if the economy be fairly integrated, not in the sense necessarily that most of the processes are horizontally or vertically under one management, but in the sense that 'at a touch' almost, a stimulus at one point must set in motion, the mechanism that will produce the infectiously growing output and employment. Instead, our awareness of 'primitive' economies is rather that for various reasons (e.g., capital being shy ; risks being high ; technical difficulties etc., being more involved ; the new developments expected often not being present even in embryo form but needing to be given birth to, and so on), and new investment or enterprise may well be only a high-souled adventure, and at best halting and clumsy.



We shall learn below more of the inevitability of the need for 'comprehensiveness' in planning."<sup>1</sup>

( ii )

It would seem clear, therefore, that some more concrete steps by the State are required. The same point as we have raised has been found reiterated in other studies and the virtual certainty of this induced rise in imports has been recognised.<sup>2</sup> The solution has been offered that "the appropriate measures would be higher-income taxes, import prohibitions or higher duties, and perhaps also increased excise taxes on domestic and foreign luxury goods alike."<sup>3</sup> While no exception could be taken to discriminating measures against luxury goods and the like, it is well to note, that higher-income tax etc., (in practice it may mean a good slice of the investible incomes) would itself present the State with no option but State planning and development. Besides, the income tax may not fall on just those groups that are in receipt of the new purchasing power. It is not on this, however, that we, any way, rest our argument for the degree of State action we are going to recommend but on other reasons ; which anon.

In addition to capital sunk in the utilities referred to and the financial facilities required, one of the first tasks of industrialisation is to provide for training and 'skilling' of labour.

This is to transform the surplus peasant population (disguised unemployment and under-employment) into full-time or part-time industrial workers (and also to train the agricultural labour 'left behind', in its own sphere). "The automatism of laissez-faire never worked properly in that field. It broke down because it is not profitable for a private entrepreneur to invest in training labour. There are no mortgages on workers—an entrepreneur who invests in training workers may lose capital if these workers contract with another firm." But "although not a good investment for a private firm, it is the best investment for the State. It is also a good investment for the bulk of the industries to be created when taken as a whole, although it may represent irrecoverable

---

1. My "Ceylon, Beveridge and Bretton Woods", Page 26.  
2. c.f. Buchanan, Page 550.  
3. Buchanan, Page 550.



costs for a smaller unit. It constitutes an important instance of the Pigovian divergence between 'private and social marginal net product' where the latter is greater than the former."<sup>1</sup>

Although this is a weighty argument, it is not the most important reason in favour of such a large investment unit as the State. That goes for land reform, assistance to infant industries, and so forth as well. It can still be argued that the State can do the training and the rest can be left to private enterprise.

It is really the fact of complementarity of different industries that "provides the most important set of arguments in favour of a large scale planned industrialisation." The case has been admirably put by Allen and we may well repeat it here. Suppose 20,000 hands are taken from the 'land' and put into a large shoe factory. They receive wages substantially higher than their previous meagre income in natura—and that is of course as it has to be (c.f. the physical needs when fully employed, transport costs of food etc., workers' housing room and so on). Now, if the workers spent all their wages on shoes, a market arises not disturbing the pre-existing market and "90% of the problem (assuming 10% profits) would be solved." But the trouble is that the workers will not spend all their wages on shoes. "If instead one million unemployed workers were taken from the land and put, not into one industry, but into a whole series of industries which produce the bulk of the goods on which the workers would spend their wages, what was not true in the case of one shoe factory would become true in the case of a whole system of industries: it would create its own additional market thus realising an expansion of world output with the minimum disturbance of the world markets. The industries producing the bulk of the wage goods can therefore be said to be complementary. The planned creation of such a complementary system reduces the risk of not being able to sell and, since risk can be considered as cost, it reduces costs. It is in this sense a special case of 'external economies'."<sup>2</sup> It may be added

1. Rosenstein Rodan, *Economic Journal*, June-September, 1943.

2. *ibid.* It is interesting to note Mill's formulation of Say's Law in *Essays in some Unsettled Questions of Political Economy* (L.S.E. reprint, 1948) page 73, which is in a nutshell the expression of and case for balanced growth. (Quoted by Ragna Nurkse in *American Economic Review*, May, 1952, page 572, *Some International Aspects of the Problem of Economic Development*). c.f. also J. H. Adler in same issue of *American Economic Review* page 588.



**PART III**







that while in the highly developed and rich countries, with their more variegated needs, it is difficult to assess the prospective demand of the population, it is not as difficult to foresee on what the formerly unemployed workers would spend their wages in regions where a low standard of living obtains.

The need for complementarity is further emphasised by some of the problems mentioned in Chapter 6 like the population factors, modern wages and working hours, absence of free markets, lack of pre-industrial capital, and the terms of trade.

( iii )

There are also certain very useful objectives that the development plan should have in mind in nursing the changing structure. One of these is that the development should be planned throughout to take advantage of the 'external economies'. The term as used here implies a vast amount more than might be understood under a system of individual commitments. In addition to the Marshallian economies to the firm within an industry, there are also in the same manner the external economies to an industry within a system of industries.

"It is usually tacitly assumed that the divergence between the 'private and social marginal net product' is not very considerable. This assumption may be too optimistic even in the case of a crystallised mature competitive economy. It is certainly not true in the case of fundamental structural changes in the international depressed areas. External economies may there be of the same order of magnitude as profits which appear on the profit and loss account of the enterprise.

"Finally the existing institutions of international and national investment do not take advantage of external economies. There is no incentive within their framework for many investments which are profitable in terms of 'social marginal net product' but do not appear profitable in terms of 'private marginal net product'. The main driving force of investment, the profit expectation of an



individual entrepreneur, is based on experience of the past.<sup>1</sup> Experience of the past is partly irrelevant, however, where the whole economic structure of a region is to be changed. An individual's knowledge of the market is bound to be insufficient in this case because he cannot have all the data that would be available 'to a planning board.'

His subjective risk estimate is bound to be considerably higher than the objective risk."<sup>2</sup>

Besides, if the industrialisation of international depressed areas were to rely entirely on the normal incentive of private entrepreneurs, the process would not only be very much slower, the rate of investment smaller and (consequently) the national income lower, but the whole economic structure of the region would be different. Investment would be distributed in different proportions between different industries,<sup>3</sup> the final equilibrium would be below the 'optimum' which a large planning body could achieve. "In the international capital market the existing institutions are mostly used to invest in, or to grant credit to, single enterprises. It might easily happen that any one enterprise would not be profitable enough to guarantee payment of sufficient interest or dividend out of its own profits. But the creation of such an enterprise, e.g. production of electric power may create new investment opportunities and profits elsewhere, e.g. in an electrical equipment industry. If we create a sufficiently large investment unit by including all the new industries of the region, external economies

1. c.f. General Theory, Page 164. The 'inclusiveness' of the General Theory as such seems vindicated once more in this case. "I expect to see the State which is in a position to calculate the marginal efficiency of capital-goods on long views and on the basis of the general social advantage, taking an ever greater responsibility for directly organising investment."

2. Rosenstein-Rodan, loc cit.

3. The terms Production for Use and Production for Exchange or, better, Profit, have been the subject of so much heated controversy that they are best avoided. It may however be mentioned that Maximum Profit is not necessarily a correct indication at all of economic (not merely social) desirability. Profit, in so far as it is a function of existing demand streams, is the creature already of a given pattern of income concentrations. Several lines exist, especially in under-developed countries, essential to ultimate viability of the economies but at whose ends the income concentrations are weakest; and vice versa. Entrepreneurial investment in 'Commerce' to satisfy import demand for luxury goods is a simple



will become internal profits out of which dividends may be paid easily."<sup>1</sup>

We may emphasise, then, that the difference between the two systems is the implicit point that "the whole of the industry to be created is to be treated and planned like one huge firm or trust" ; and that "an institutional framework different from the present one is clearly necessary for the successful carrying out" of the industrialisation.

One important point may be added here. The new structures must be such that both the interest or dividend services on foreign loans and the repayment of loans must be assured. For this, one part of the industries created will have to be export industries. "The flow of their exports will have to be sold in creditor countries. These exports will represent the main part of the rich countries' share in the world expansion. The placing of these exports has to be foreseen and planned in such a way as to minimise the burden of necessary adjustment of economic resources in the creditor countries."<sup>2</sup> Probably, processed foods and light industrial articles (including tea and worked up rubber and coconut) will play a leading part in this trade. Competitive abilities, elasticities of demand and supply and terms of trade will be important factors. The limits to the amount that must be borrowed or can be borrowed have to be understood in relation to these determining factors. We shall come to this point again later.

( iv )

This may also influence the financial method to be adopted in implementing a programme of development and be decisive in determining the degree of State action required. Development

---

but ample illustration. c.f. Lewis, *Principles of Economic Planning*, page 21. "Fundamentally, where planning parts company with laissez-faire is not in rejecting the market economy controlled by demand, but in arguing that demand itself is not sacred . . ." The same point is referred to by John H. Adler (in *American Economic Review*, May, 1952 page 592, when he refers to the 'skewed distribution of income.'

1. Allen c.f. Lewis, *Principles of Economic Planning*, page 125. "In these days if one wishes to develop secondary industries, one must do it on a large scale, and deliberately set out to create the facilities which factories use in common, and which cannot be provided cheaply on a small scale. That is why the trading estate, financed by government, is now the established technique for developing depressed areas."

2. Rosenstein Rodan, *loc cit*.



could be done for example on the Russian model—by which is not meant communism—“aiming at self-sufficiency without international investment. That would imply the construction of all stages of industry, heavy industry, machine industry as well as light industry, with the final result of a national economy built like a vertical industrial concern.”<sup>1</sup> There are however, said to be grave disadvantages. (a) It can only proceed slowly, because capital must be supplied internally at the expense of a standard of life and consumption which are already at a very low level. It implies, therefore, a heavy and unnecessary sacrifice. (b) It will lead finally, since there are appropriate natural resources in the area, to an independent unit in the world economy implying a reduction in the international division of labour ; i.e. the output of the world as a whole would be less than it might be, the world would be poorer in material goods. (c) The difference in world economic structure is most clearly seen in the case of heavy industries. Building up heavy industries at a great sacrifice would only add to the world excess capacity of heavy industry, and would constitute from the world’s point of view largely a waste of resources. We do not mean, however, by such censure that no agricultural country can adopt such a method with profit. It depends on the size of the unit ; the possibility of the desired cut in consumption, under capitalism ; and related factors. The fact that Russia did it, cannot automatically mean that all other countries (as they are today) can. Yet, the fact that with a socialisation of the means of production the task is easier, may itself be the argument for ‘sovietising’ the system. The imperativeness of the need for it may vary with the type of the co-operation afforded by the other political powers in implementing the programme.

The alternative way of industrialisation of course has the conventional advantage named, of fitting the units “into the world economy, which would preserve the advantages of an international division of labour, and would therefore in the end produce more wealth for everybody.

It would be based on substantial international investment or capital lending.” This way, given the most probable political situation in the post-war world, can present several advantages :

---

1. *ibid.*



“(a) It could proceed more quickly, and at a small sacrifice of consumption of (the) area. From the point of view of international political stability there may be all the difference in the world if 50% of the agrarian excess population . . . were profitably employed within ten years after the war instead of say 20%. (b) The sound principles of international division of labour postulate labour-intensive, i.e. light industries in over populated areas. (c) Even for the purposes of an expanding world economy, the existing heavy industries in U.S.A., Great Britain, Germany, France and Switzerland could certainly supply all the needs of the international depressed areas.”<sup>1</sup>

The fact, however, that savings can be supplemented by ample capital borrowing presents, as mentioned, a dangerous situation. The deficit intelligently created must be rectified when the transition has been effected. That, in any case, the amount that could be borrowed will be only a fraction of the entire costs of industrialisation is evident from the following. In the words of a writer referred to before<sup>2</sup> “According to one careful estimate the 8.5 million wage earners in American manufacturing industry in 1937 worked with 21.2 billion dollars of capital assets, other than land, or an average of 2,474 dollars per wage earner.

Also in 1937 the total population of the continental U.S. was estimated at 128.8 million persons. Consequently the investment in capital assets other than land in manufacturing per head in the U.S. was 164 dollars. Now to add to the capital investment in manufacturing in India with its 400 million persons an amount of 20 dollars per head (and assuming no growth in population to occur in the process) would require an investment of 8 billion dollars. An increment of this amount, of course, would leave India still far behind the U.S. in capital equipment in manufacturing. Furthermore without similar investments in transportation, warehouses, distribution facilities etc., the investment in manufacturing would be of limited usefulness. The sheer magnitude of the capital sums required show that only a small fraction of the investment required for industrialisation can come from abroad under any reasonable assumptions.

---

1. *ibid.*

2. Buchanan, Pages 548-9.



A more important reason why only a small fraction of the total investment necessary for industrialisation can come from abroad is to be found in the nature of the real Capital needed. Any industrialised country has a high proportion of its total productive Capital in the form of buildings, railway road bed, highways, harbour developments, sewerage systems, river developments and the like which by their very nature cannot be 'imported' in any direct sense. They have to be fabricated on the spot by local labour using local materials. Except for the rails and crossties, a railway line from the sea coast to the interior in an under-developed country cannot be imported ; it has to be constructed locally. Any assistance from abroad must be indirect in projects of this sort. And a very large proportion of the Capital goods needed for industrialisation are of this type."<sup>1</sup> A quotation by this author significantly adds that 'most of the capital goods required in the industrialisation of Japan were produced domestically.' It would thus appear that State action cannot stop with responsibility for arrangement of external help. There is considerable internal activity required for development for which State intervention and participation may become essential.

In so far as loans are required, the Bombay Plan presents a fair illustration as to the manner in which they may be utilised. Although the Plan is now only of academic interest, it may be said to have influenced present trends in Indian economic policy.

The cost of the plan is put at Rs. 10,000 crores. The following are the allocations made, for the 15 years of the plan, in terms of Balances, Capital, Saving, and Additional Currency :—

	Rs.	(Crores)	£	(Millions)
External Finance				
Hoarded wealth ...	300	} (1900)	225	} (1425)
Sterling securities ...	1000		750	
Balance of Trade ...	600		450	
Foreign borrowing ...	700		525	
		2600		1950

1. Of course, the whole of consumption needs during development could be imported on loan bases and in this sense foreign capital can be made to form a substantial proportion. In practical terms, food and clothing could be largely thus imported. The question of limits is further discussed in the Chapter on Planning.



## Internal Finance

Savings ...	... 4000	3000
Created money	... 3400	2550
	<u>7400</u>	<u>5550</u>
	<u>10000</u>	<u>7500</u>

“The total expenditure on basic industries over the whole period is estimated at Rs. 3,480 crores (£2,610 millions). A large proportion of this will have to be spent on the import of foreign capital equipment” and though “the total amount of external finance which is likely to be available to us is, however, in the neighbourhood of Rs. 2,600 crores (£1,950 millions) only, the expenditure on basic industries during the first two plans which amount to Rs. 1,680 crores (£1,260 millions)” is well within the limits of the “external” finance (leaving out foreign borrowing as well); and, say the Bombay Planners, “we presume that the basic industries which would be developed in the first two plans would be such as would themselves produce a substantial proportion, if not the whole of the capital equipment needed for the basic and consumption goods industries to be developed in the third period.”<sup>1</sup>

Meanwhile, savings and new money will be utilised in regard to the other items of development in these ten years. In the last Five-Year period, borrowing will probably gain increasing importance. When we compare the figure for saving and that for borrowing we see the ‘minimum’ to which the latter has been reduced. Not all countries however are lucky to have foreign balances. However, the above gives some indication of the procedure to be adopted in tapping the various sources. Whatever the wisdom of the above, it is necessary for all agricultural countries consistently with their divergent conditions, to adopt some such classification as a prelude to effective action.

1. The Plan (Penguin edition).



To go back to the question of state participation,<sup>1</sup> we may say that planning through Investment Boards seems very essential. The need to treat the economy as a huge firm or trust is urgent. Foreign borrowing is better at Governmental levels, and in any case has to be regulated and controlled by the State.

Further, such loans should always be tied to import of technical skill and capital goods proper.<sup>2</sup> But the mechanism of finance need not be all State; rather an incorporation of public finance through a series of Public Corporations,<sup>3</sup> at every possible stage is the desideratum; and giving free room in sectors wherever private hands are expected to be willing and able to undertake responsibility,<sup>4</sup> so long as such activity does not run counter to the postulated trends and lines of development. In fact, if the State were to do everything, there may as well arise a case to abolish the present basis of society and to nationalise all factors of production. The latter is the only basis on which the State can properly do everything; but as we said, the State need not necessarily do everything.

1. c.f. Buchanan, Page 552. "Thus the road from lower to higher per capita incomes via industrialisation has its obstacles. The Nineteenth Century sequence will probably not be repeated. The State rather than the drive of private enterprise in pursuit of profits will determine the major features of industrial development in the (now) low income areas. Domestic savings and investments, labour training and mobility, imports and exports, foreign borrowing and home finance will be guided by the visible hand of the State in the quest for higher incomes, through industrialisation."

2. On the flow of funds from outside, it has been pointed out, that so far as the U.S. is concerned, experience in the inter-war period shows that direct investment was not subject to business cycle influence to as great an extent as the more formal type of investment abroad in loans.—Economic Journal, March 1946, Page 87, Yuan-Li Wu.

3. A feature that is well worth study is the theory of 'co-operative production', whereby the workers in an Industry as a whole would own and run it. This is what was demanded by early British Socialists. This is different from the position in the nationalised industries in Britain today, which "belong to the public, who will employ the miners, and the essential relation is not changed by the change of ownership." Besides, "decentralisation is desirable in the interest of efficiency, because enormous corporations are difficult to administer from a single centre. It is also necessary if the participation of workers in management is to be real... it is not desirable that nationalisation should be an instrument for increasing monopolisation... Ministers should exercise very little control over corporations" Lewis, op. cit. pages 100, 103 and 105.

4. In chapter 12 we discuss the feasibility of State determination of production lines in under-developed countries. There is a fringe, which becomes the major sector in an advanced country living on exports of 'skilled' goods, wherein State enterprise is likely to be stifling. England, it is said, can hold her own today if she is "constantly in the vanguard pioneering new ideas, inventing new goods and processes, trying them out on the market, adjusting rapidly in accordance with consumer reaction, and so on." This involves freedom of entrepreneurship to proceed despite all opposition and to get its resources without hindrance. W. A. Lewis, Principles of Economic Planning, page 18.



**PART III**







## CHAPTER NINE

# The Structural Set-up in Two Agricultural Countries

### Countries Selected

THE countries to which we have chosen to confine ourselves, namely the over populated low-income types, may not be wholly representative since they do not come under the category of the more prosperous agricultural economies. The problems in the former are, however, more varied and more comprehensive. The selection of India and Ceylon from among these is also appropriate in more than one way. One is an extremely large country ; the other a very small one. Foreign trade plays an overwhelming role in the latter economy, the state of capital development is low, and the internal market is small. These may well induce different and varying policy decisions in regard to economic development and full employment.

### Purpose of this Chapter

We shall analyse the structures, broadly in terms of primary, secondary and tertiary groups. We shall demonstrate the overwhelming predominance of agriculture and the peculiar difficulties in its present organisation, and illustrate subsequently the relative insignificance of the other groups, especially of industry.

It will be found that the need for an Investment policy is brought out by the study.

### Under-employment

In Chapter 3 of this Book we considered certain important characteristics of agriculture as such. Among them were the degree of adaptability of supply, location of produce, size of the unit and amount of capital, the role of the middleman, and the earning capacity of agriculture. We also considered the part played by the State in steadying and improving conditions. We



have, however, not mentioned, except in passing, the crucial problem of under-employment arising from pressure on the land. In India and Ceylon this is an over-riding feature. So much so, that the questions mentioned above could be explained in terms of this alone. We shall, therefore, first make clear what is meant by this problem of under-employment.

The two crucial concepts in modern Full Employment Theory are Full Employment and Unemployment. The term under-employment has been used to describe certain situations, but these situations were never considered of overwhelming importance. Unemployment remains the prime concept in advanced economies. Equally, however, under-employment is the prime one in backward economies. Both are related to what may be called the total general capital equipment in the economy. They are also justified in their use, as terms, by this latter. If the existing capital equipment in the economy is such that, despite partial disuse at the moment, it is capable of absorbing the total working population, or of expanding sufficiently in the process to take on the numbers seeking work then the problem is not one of under-employment but of unemployment. If the economy's total capital equipment is insufficient for the purpose, and is also unable to add to itself under influence of general policies for revival, the problem is one of either chronic unemployment or chronic under-employment. The stagnationist theories of the thirties went nearest to talking of the former in advanced countries. In the agricultural country the disequilibrium was not a manifestation of a phase but a permanent characteristic rooted in the nature of its activity and in the pressure of the population.

When we say that the existing capital resources and land cannot absorb the existing volume of labour we have to understand it in an economic sense. For the agricultural economy does, physically speaking, absorb its labour supply. That is what distinguishes it from unemployment. Under-employment has to be explained in terms of working hours, or of number of workers required to produce the optimum amount, or of potential better employment available in alternative sectors of production. In a developed economy too there can be less than full employment per worker, for instance when the number of shifts is reduced in industry and



the job is spread over more hands. This under-employment is not, however due to inadequate capital and organisational structure as it is in the agricultural economy.

We shall see that, in terms of providing work to occupy full hours, in terms of producing the maximum from the land and in terms of utilising the higher income prospects elsewhere, the present organisation is unsatisfactory. Accordingly, the recommendations in the next chapter will take into account the provision of subsidiary occupations on the farm, the creation of conditions for higher productivity, and the seizing of opportunities for more productive work in the other sectors.

It is extremely difficult to measure the degree of under-employment accurately. One needs to accept a norm, like an eight hour day, and dismiss shorter or longer hours as departures from full employment. If a pressure on the land were caused by all the factories working a twelve hour day, or extra shifts confined to a restricted labour force, the disequilibrium could not be described as fully one of under-employment. In terms of optimum output, though on a comparison with other countries the existence of under-employment could be demonstrated, the exact measure is difficult to make. An estimate attempted in terms of land required for a family to enjoy a postulated standard of living is only partly satisfactory and hardly useful in formulation of policy. The productive capacity of the family is measured under conditions of existing imperfectness in holdings, poverty of capital equipment and so on. The calculation cannot take into account the effect on this capacity of the new earnings in other sectors created by the exodus from the land.

The capacity is also dependent on the amount of the exodus that is possible into the other sectors without reducing levels of earnings in them below the level postulated for the farm units. We shall not, therefore, attempt to illustrate the problem except in broad general lines.

Under-employment can be divided into types. The organisational or structural is the result of pressure of population, nature of the land system, inadequacy of capital and so on. The seasonal



type is caused by the inactivity in agriculture during certain seasons. Not the whole need necessarily be designated as under-employment, since in several areas two-season cultivation may not be undertaken when it could be. It is said that in India a second sowing is often done only when the main crop fails.<sup>1</sup> In Ceylon, except in the Peninsular North, most of the processes of manuring, transplanting, weeding, and so on, are either not done or imperfectly done. In assessing the amount of farm labour that may be considered 'surplus' one must needs make allowance for these factors. But the number of people required at the height of the season should not be taken as the minimum required on the land. For one thing, modernisation can well reduce this number considerably; for another, there is a seasonal flow into the land. Assuming a suitable dove-tailing of occupations, this latter movement should be retained. For instance, a tendency has been noted in Ceylon for fishermen to help in agriculture during their 'off-season'. Caste system proves a great hindrance, but it would appear that slowly, even imperceptibly, the change for the better is on the way. When all is said, and the minimum required on the land is agreed on, still there are 'slack' times. In Ceylon the longest period is four months.<sup>2</sup> Idleness among female hands is also considerable.<sup>3</sup> This seasonal unemployment is natural to agriculture and only subsidiary occupation can take up the slack. The problem in India and Ceylon, however, does not seem to be merely one of this basic under-employment, but much more a true 'surplus' on the land.

Seasonal movement in labour supply should not automatically be associated with under-employment. As mentioned, the movement of population from neighbouring areas, or countries, at the height of the agricultural season, does not mean under-employment to these migrant hands in the 'off-season'. The so-called off season is often the season for other activity—instead of reaping, or 'picking hops or vine', they may be hauling goods

1. c.f. I.L.O. "The Economic Background of Social Policy—including problems of Industrialisation." Report prepared for the Asian Conference in Delhi, 1947.

2. Sess. Paper 11 of 1950. "Agricultural Wages & Earnings of Primary Producers in Ceylon".

3. c.f. e.g. The Annual Reports of the Lanka Mahila Samiti; a State-recognised women's society which has played a considerable part in rural welfare and development work over the last 21 years.



at ports or warehouses or doing some 'urban' job. This fitting of activity in other sectors to the 'seasonal rhythm' of agriculture is, within limits, healthy and desirable. Where, however, labour moves from industry during a slack season, to the land, irrespective of the latter's demands, the position is different. (The converse position is where labour moves from the land to industry during the slack season in agriculture). It increases under-employment on the land; it is temporary; it is not caused by agriculture. It will be more appropriate to use the phrase disguised unemployment for this, or to call it seasonal under-employment in the secondary sector. The remedy has to be sought in the latter. Where the exodus to the land is due to depression in industry, the term disguised unemployment is even more fitting. It is this process that operates in the plantations, for instance, in Ceylon. World slumps caused considerable 'migrations back' of the indentured Indian labour to their homes, and revivals brought them back again. They must have increased pressure on the land in India. The crux of the problem was however, in the plantations.

The extent of under-employment in India may be shown partly by the size of the holding and partly by the level of the per capita incomes. The average size of the farm in several provinces in India is under five acres. This may be compared with the figures of 145 acres in the U.S., 40 acres in Denmark, 20 acres in England and so on.<sup>1</sup> On the other hand, cultivated land per head of population, which is .9 an acre, is not much different from the corresponding figures for France, Germany, Italy and England, while the cultivated areas per head in the U.S.A. and the U.S.S.R. (2.7 and 2.0) are not very much greater.<sup>2</sup> (In S.E. Europe figures as high as 2.96 and 3.21 have been mentioned, reflecting probably a considerably larger size in farms compared to India). The general impression from the figures is that the population is not necessarily more than the land can be made to feed, but that no reasonable portion of this population has shifted itself to other sectors of activity, as it has in other countries in the West. The average size of holdings in a village in the Poona District is stated as having been 40 acres in 1771, 17½ acres in 1818, remaining stable at 14 acres from 1820, but going down to 7 acres by 1915.<sup>3</sup>

1. I.L.O. loc. cit. page 33.

2. Ibid. pages 21, 22 and 23.

3. Jathar and Beri in 'Indian Economics' quoting Dr. Mann.



The decline of handicrafts and the laws of inheritance made this appear inevitable. The increasing population was, of course, a fundamental factor.

Intimately related to the size of the holding is its normal accompaniment, fragmentation. In the village referred to above, 156 owners were found to have 729 plots of which 463 were less than one acre and 211 less than a quarter of an acre. The extents to which these could go are shown by figures of .00625 an acre in places, or fields one mile long and a few yards wide, or even cases where cultivation is entirely prevented.

Estimates of per capita income in India are at variance with one another and it is possible to set down the position only in a general way. The following figures have been mentioned Rs. 115 (1942-3),<sup>1</sup> Rs. 301 (48-49),<sup>2</sup> and Rs.  $62 \pm 6\%$  (1931-2).<sup>3</sup> Allowing for official under-estimates, taxation, etc. the last figure should be Rs.  $65 \pm 6\%$ . Price movements of course, account for a good part of the difference. For instance, the figure for 48-'49 at '45-6 prices is given as Rs. 200.<sup>4</sup> Rao's figures have the merit of being explained in detail, more comprehensively gathered and more fully scrutinised than some earlier ones, including his own of 1925-9. On his estimate, per capita rural income (allowing for under-estimates, etc.) is only Rs. 51 while urban income is Rs. 166.<sup>5</sup> That this is a very low level is clear, especially when about 70% of the population depend on the land for livelihood.<sup>6</sup> It would be fair to infer from these that under-employment is a grave problem in the economy.

The per capita income in the U.K. is over 10 times, and the U.S. nearly 20 times as large.<sup>7</sup>

### Productivity in Agriculture

The productivity of labour is broadly determined by the corresponding supplies of labour on the one side and land and capital

- 
1. Econ. Survey for Asia and the Far East, 1949. (Ecafc) page 17.
  2. The Colombo Plan (H. M. Stationery Office). page 69.
  3. V. K. R. V. Rao. National Income of British India, 1931-2, pages 185-6.
  4. Col. Plan. page 12.
  5. Rao. page 188.
  6. Col. Plan. page 12.
  7. Col. Plan. page 10.



on the other ; by the arts of production ; and by the degree of 'skill'. Continually increasing numbers on the land, working *with the same means of production* naturally lower output. Increase in means of production depends on capital formation, which, in the absence of increasing employment in the secondary and tertiary sectors, is bound to be quite small. The lack of capital has affected water conservancy, flood control, soil conservation, irrigation, drainage and transport. It has affected introduction of better and more efficient equipment, seeds, manure, and cattle on the farms. But even if capital supply had been more satisfactory, their use on the land and the improvement in production methods would have been obstructed by the problems of subdivision and fragmentation. The high cattle population in India (estimated at  $\frac{1}{3}$  the recorded figures for the world) signifies a capital cost out of proportion to the small size of the unit. Similar objections arise in regard to fencing and sinking of wells. In the result, the farmer gets mostly the worst of both worlds, a tendency particularly emphasized when both subdivision and fragmentation exist together. Use of labour saving devices is generally prevented and the adoption of really intensive cultivation is hindered. The expenditure of capital and labour is greater than if the unit were larger or in one compact block. "It is calculated that the expense of cultivation increases by 53% every 500 metres of distance for manual labour and ploughing; from 20 to 35% for transport and manure, and from 15 to 31% for transport of crops."<sup>1</sup> In China the production of one quintal of rough rice is estimated to require 4.55 working days of 10 hours a day, and only 0.3 days in the U.S.<sup>2</sup> Or again, India's cultivated area is 306 million acres, that of the U.S. 360 million. India has 73 million workers on the land, the U.S. 8 million. The yields per acre in India are extremely low. U.S.A. has 2,400,000 tractors, India 10,000 ; the U.S.A. uses every year 13 million tons of fertiliser ; India 200,000.<sup>3</sup>

Debt is a feature natural to agriculture. In India, however, its proportions are alarming. The low incomes call for borrowing for most capital purposes. But the overwhelming reason for debt has been to meet consumption. Besides, borrowing is at

1. Jathar & Beri. page 182.

2. I. L. O. op. cit. page 39.

3. Colombo Plan page 10.



very high rates of interest. Reduction in size of holding or outright loss of land is a necessary consequence. It is notable that a high average debt per family (Rs. 242) was discovered in Assam where the average size of the holding is 3 acres, and a much lower debt (Rs. 32.9) in Bombay with an average holding of 12.2 acres.<sup>1</sup> According to an estimate of the last century, 1/3 of the land holding class were deeply and inextricably in debt, and at least an equal proportion, though not beyond the power of recovery, were also in debt.<sup>2</sup> As a result of the war much of the debt is said to have been wiped out. Since it is inflation and not real productivity, however, that enabled this result, the basic serious instabilities in agriculture continue to exist.<sup>3</sup>

Efforts by law, administrative action, conciliations, compulsory State action, assistance in finance, and by co-operation have for years been made.<sup>4</sup> In limited areas impressive successes have been recorded. The Agricultural Commission of 1929 thought that if co-operation failed, there would fail the best hope of rural India. In every field of the farmer's activity, the methods of co-operation have, given the chance, proved their worth.

Rents are an important feature in India for two reasons. An overwhelming portion of the land is held by tenants; and absenteeism is very prominent among the landlords. The average rent is estimated at 50-60% of gross produce, while conditions for the sharecropper involve performance of other services as well.<sup>5</sup> The burden is made heavier by the fact that it is only in some areas that the landlord provides any equipment or arranges irrigation facilities. It has been remarked that 'next to War, Pestilence and Famine, the worst thing that can happen to a rural Community is absentee landlordism!'<sup>6</sup>

1. I. L. O. op. cit. page 36.

2. Jathar & Beri. page 253.

3. Eastern Economist, August 27th, 1948, page 375. "It is worth noting though that (in Madras Province) between 1930 and 1946 the gross reduction of debt was Rs. 82 crores—of which Rs. 10 crores was due to the operation of the Agricultural Debt Relief Act, about Rs. 47 crores due to the sales of land and only Rs. 25 crores to the war-time rise in prices."

4. Recent steps, e.g. in Bombay, include the licensing of moneylenders and limitation of interest to 6%.

5. I. L. O. op. cit. page 43.

6. Jathar & Beri, page 220.



Land is cultivated in India as Zamindari, Mahalwari (joint village or village community) or Ryotwari.<sup>1</sup> This arrangement was crystallised through the Settlements first instituted in Bengal under British rule. This has been the basis for the land revenue system in India. The system has been no doubt responsible for bias in favour of investment in land rather than industry, as well as for over capitalisation of rent receiving, evils of absenteeism and of sub-inefficiency. In the case of temporary settlements, there was a deliberate neglect of the land to escape enhancement of payments, and consequent deterioration of land near the end of the settlement term. There seems to be a movement now to introduce agricultural income tax, which is of course more to be commended than the Settlement system. The chief point about the Land Revenue was that payments were not progressive. The abolition of Zamindari<sup>2</sup> has been taken up in several provinces, with Madras giving the lead. Much of the ultimate usefulness of this measure depends on the degree of subsequent assistance given to the peasant to protect his new economic position.<sup>3</sup> It will involve also providing healthy avenues of investments for the financial compensation granted to the Zamindaris.

Marketing is one of the worst aspects of agricultural organisation in India. The long chains of middlemen, forward contracts with a debt-ridden peasantry, inadequate communications have all had serious effects. It has been observed that 'out of a rupee which the consumer pays for his wheat, the producer gets 9½ annas'. According to a more recent report on the marketing of rice in India,

---

1. In 1921 there were 291 agricultural labourers to every 1,000 cultivators; in 1931 there were 407. The reasons assigned were population growth and concentration of ownership in non-cultivating owners. (India Analysed by Maini and others).

The Zamindari, supposed to take only a little more in rent than he paid to Government, has in fact taken anything up to 40 times the land revenue. And evictions ran into thousands a year. Another noteworthy feature is that there has been an average of over 1 million transactions a year in sales and mortgages in 1925-45, and one and a half million in 1943. "Hardly the static countryside of the romantic imagination." Economist, November 19th 1949. Page 1126, and March 4th, 1950, page 489.

2. The Zamindari Settlement has been described as "a gigantic British misunderstanding"—Economist, March 4th 1950. Page 489.

3. One anomaly even of the reform has been mentioned. Bombay and Madras are predominantly ryot-wari areas. While the Ryots and Tenants Protection Act of 1946 (Madras) prevents the Zamindar from evicting a tenant who has paid two years' rent, there is nothing to prevent a ryot-wari land owner from doing so. "Swatantra"—Madras Journal, January 3rd, 1948, Page 19.



'the cultivator gets only  $8\frac{1}{2}$  annas of the rupee paid by the consumer'.<sup>1</sup> The bargaining power is on the side of the middleman. Weak selling has become a marked feature of the system. This bargaining power is greatly influenced by the rural indebtedness earlier described and by the social structure. The middleman has generally the resources of both wealth and more advanced knowledge of the world. The peasant has neither. This is a feature strongly brought out, for instance, by the work of the Co-operative movement in Ceylon. It is certain that the same holds for India.

### Secondary and Tertiary Sectors

India has been described as a rich country inhabited by poor people.<sup>2</sup> A long list of actual produce as well as resources can be mentioned where she holds a dominant position in relation to other countries.

Only a small fraction of her total produce is however exported. Yet, considerable amounts of rice and wheat had repeatedly to be imported. For a predominantly agricultural country, the inability to expand output to meet its own needs, betrays defective integration in the structure, made worse by lack of diversification.

To have a better idea of the problem, therefore, we may refer to the Industrial contribution in India. The contribution, to the National Income, of industry is a minor fraction. Organised industry accounted for only 16.1% in 1942-3. Even together with unorganised industry it was 27.6% of gross National Income.<sup>3</sup> It is estimated that the total number of industrial workers, including those in minor works, is about 3 million; excluding the latter, it is nearly 2 million.<sup>4</sup>

The location of India in the late 18th and 19th centuries as a producer of agricultural commodities for world trade led to the decay of the traditional handicrafts. The extremely advanced handicraft technique was the basis of Japan's industrial achievement.<sup>5</sup> The beginnings of modern industry in India were roughly

- 
1. Jathar and Beri—op. cit.
  2. Lokanathan—Industrialisation of India.
  3. Ecafe Report 1949. Page 14.
  4. Lokanathan—Industrialisation of India.
  5. c.f. G. E. Hubbard—Eastern Industrialisation and its Effects on the West.



in the middle of the nineteenth century. The major fillips were provided partly by the first World War, then by Protection and even more markedly by the last War. There is today a considerable range of heavy and consumer industries in the country.

The low standard of living however, is testimony to the fact that the role of industry is hardly as significant as it should be. Industrial income per worker was in 1930-31 only 50% higher than agricultural income per worker.<sup>1</sup> The following pre-war figures of average income per head, per annum for other countries may be mentioned in comparison. The figures for Agriculture and Industry, in rupees, for the U.S. were 175 and 721, Great Britain 62 and 412, Canada 213 and 470, Japan 57 and 158, Sweden 129 and 384.<sup>2</sup>

The inability of industry, by itself to expand to meet the needs of the situation—or even to do so under the stimulus of accepted full employment ‘devices’—is due to several reasons. For one thing there is a vicious relationship with low incomes causing low output and low output causing low incomes. Incomes, capital, markets and opportunities are all reduced in an under-developed area. The wage or income earners in one line of production are the consumers of wage-earners’ output in another line; while the latter wage-earners provide the market for the former line. The income earners generally provide the capital for new investment and the condition of all of them determines the general opportunities. The general atmosphere causes ‘Shyness’ of capital. Meanwhile several ‘initial major barriers’ remain unsolved. With labour unskilled, external economies limited, and presence of ‘fixed factors’ and ‘indivisibilities’, the initial discouragement is greatly magnified.

There are also other features, of an institutional nature, which emphasise the lack of diversification and integration we referred to in an earlier chapter. The capital market suffers from serious defects. In rural areas, most of the borrowing is done from local money-lenders who have charged anything up to 300% interest

---

1. Rao. Page 188.

2. Sessional Paper XV (Ceylon) of 1946, page 13.



and in several cases do charge from 50 to 100%.<sup>1</sup> The amounts provided by the Provinces and the Co-operative Societies is relatively small. In urban areas, the supply is more satisfactory, but the existing banking system is still too inelastic for industrial finance. The Imperial Bank is precluded from supplying long term finance to industries and loans against mortgage of immovable properties, even after the Reserve Bank came in. Where joint stock banks entered into such business they are said to have sunk an excessive proportion of their funds in a single industry. The overwhelming feature about industrial capital is however the large dependence on Managing Agents for working as well as initial capital. They earned a minimum commission, plus a commission on production, on sales and on profit. They would not strike out on new lines unless high profits were assured.

In the economic background already described, this slows down response to full employment measures.<sup>2</sup> The banks lend to industrial companies mainly on the credit of these Agents. In the words of the Central Banking Enquiry Committee 1930-1, the system is 'the Indian substitute for the well organised capital market and industrial banking system of Western countries and has come into existence by sheer force of circumstances.' They perform the functions of Issue Houses and Underwriters. For very large enterprises whose requirements are beyond the resources of any single Managing Agent and for smaller businesses which will be unable to attract the Managing Agents some other system of finance is required.

---

1. R. D. Tivari, *Indian Agriculture*, page 271.

2. Lokanathan—*Industrial Organisation in India*. Also c.f. Swatantra, January 31st, 1948, Page 23—Apart from genuine limitations there are also several other drawbacks in the system as evidenced by the following statement of the Industrial Tribunal on conditions of labour in the textile industry in Madras Presidency. "Dividends to the extent of about 50%-60% had been normally paid during the last three years. 'The managing agent's commission alone in a large number of cases exceeds the total wages, salaries and bonuses paid in 1943-44.' The depreciation fund is more than enough to purchase even new machinery and to replace wornout parts. Besides, large amounts have been set apart for research on textiles. But if we turn to the other side of the picture, to the share of labour in this phase of booming profits, we are amazed at the incredibly low wages obtaining in industry....So far as other social amenities of the Indian worker, such as workmen's compensation, medical care, old-age pensions, etc., go, the less said the better."



The need is for Issue Houses, and for Long and Short Term Credit facilities. Through the initiative of some Managing Agents in recent years, financial institutions have been floated with the object of starting and advancing new enterprises, both big and small. New issue and finance houses have been established in Bombay. Investment trusts have also been established in some important industrial centres.<sup>1</sup>

In the words of the External Capital Committee 'a vast store of dormant capital' exists in the country. It may also be noted that the State has been an investor in a large way in India. It is responsible for the large irrigation schemes. It is the author of several hydro-electric and multipurpose projects and owner of the railways and main highways. A system of Industrial Finance Corporations by the State is being introduced. Under recent legislation, the Reserve Bank is given wide powers of control and direction over the banking system. The present level of capital formation is, however, very low.

The inadequacy of transport facilities is a considerable hindrance to development. Neither the imperfections of location and size, nor those of distribution charges, could be well tackled with the inadequate transport. The square kilometer of Area and Number of People per Kilometer of Railroad were 61.9 and 5,878 (including Pakistan).<sup>2</sup> Compared to conditions in advanced countries there is much headway to be made. The deficiency seems even greater in regard to highways. We noted, in an earlier chapter, that location in agriculture is not strictly determined by the so-called Von Thunen zones, but that units tend to be established along rivers, roads and similar lines of communication. The deficiency in communications in India, prevents both efficient marketing and mobility of labour. It creates isolated pools of supply, each its own market and each subject to violent fluctuations of prices. In China, it is said, while consumers in one region are threatened with famine, farmers are ruined in another because they cannot dispose of their surplus.<sup>3</sup> While this may not be strictly true of India today, it is reasonable to imagine situations parallel to the

---

1. Lokanathan—Industrialisation of India, page 24-5.

2. Ecafe Report 1949, page 113.

3. R. H. Tawney, Land & Labour in China, pages 55-6, 1932.



following. The cost in China of moving foodgrains 50 miles was said to be more than the price at the place where they were grown. The cost of merely moving grain from Shensi to Shanghai exceeded the combined cost of producing and importing grain from Seattle.<sup>1</sup>

The situation in urban areas in India is far better than for rural. However, even for industry its source of supply and especially its market must be served by efficient communications if the economy is to be structurally balanced.

A special feature of the tertiary sector in the economy is the large number engaged in personal and domestic service. Although only about 23% of the working population are in the tertiary group, compared to nearly 50% in Australia and the U.S.A., yet 10% of the working population is engaged in personal service in the former instance and less than 5% in the latter.<sup>2</sup> As in agriculture, a good part of the numbers in the tertiary sector are there because they would otherwise be unemployed. On the side of the employers, the extremely low remuneration for the service enables a large number of them to pay for domestic assistance.

The statistics for wage levels refer to organised industry mainly and the like, and do not indicate the position for the economy as a whole. Between 1939 (base year) and 1945, wages rose 120% in Bombay, and 103% in Madras, while the All British India figure was 107%. The cost of living index however rose to 224, 228 and 277 respectively.<sup>3</sup>

### Foreign Trade

In the sphere of foreign trade, two characteristics may be noticed. The relatively small fraction of export vis-a-vis production, and the large proportion of 'wage-goods' in the import volumes. Exports were 6.2% of total products in 1942-3.<sup>4</sup> Of the imports, wheat and rice accounted for Rs. 921 million, as against Rs. 908 million on machinery and equipment.<sup>5</sup> The import volume of the

- 
1. Op. cit.
  2. I. L. O. Report Loc cit.
  3. Ecafe Report '49, page 144.
  4. Op. Cit. page 204.
  5. Colombo Plan, page 70.



economy was more a reflection of the margin by which the country is found wanting, than of any vigour in economic activity within. The exports include large amounts of unprocessed material and exist more as a means to pay for imports necessary to maintain the subsistence level, than as the agent of a prosperous and rising standard of living.<sup>1</sup> The pressure of population has now been aided by Partition which has worsened the trade situation. In the opinion of one observer, India then was dependent for 75% of the raw jute supplies, costing Rs. 100 crores, on Pakistan. Deficiency in cotton was about 2 million bales costing Rs. 90 to Rs. 100 crores. These two items and food grains together totalled over Rs. 300 crores of foreign exchange, roughly 75% of the total exports.<sup>2</sup>

Employment in industry, together with the plantation industries can create some impressions on the economy. But the mass of the rural employed and unemployed moves in a sphere of under-employment and famine. The concepts of employment and unemployment in the industrial sense would be a travesty of the facts. The accepted full employment devices, also, become irrelevant.

### CEYLON—Rural Background

The gist of the position in Ceylon is as follows. The population at present (1951) is 7,147,000.<sup>3</sup> Two thirds of the cultivated land is taken up by tea, rubber and coconut. "80% of the people are employed either directly or indirectly in the production and handling" of these.<sup>4</sup> Two-thirds of the present restricted consumption of rice is met from imports. Food accounts for over half the annual expenditure on imports, while tea, rubber and coconut account for over 90% of export value. Almost all the clothing is imported. So also are the 'conveniences and amenities of civilised life'. The per capita income (1949) is Rs. 417, the main exports accounting for about half of it. The exports themselves are liable to wide fluctuations in values.

1. The position is in bad times made very precarious indeed. e.g. In 1939 one ton of imported food was paid for by exporting a quarter of a ton of jute or 100 lb of tea; today a third of a ton of jute or 300 lb of tea are required—*Economist*, November 26th, 1949. Page 1166.

2. Agarwala, *Free Press Journal*, Bombay. 31st May, 1949.

3. *Census of Ceylon, 1946—General Report*, Table 3.

4. U. N. Publication—"Maintenance of Full Employment" page 28.



The following are the figures of National Income, Per Capita Income and cost of living for the years 1938 and 1947-50.<sup>1</sup>

Year	National Income	Per Capita Income	Cost of Living. (Average November '38—April '39=100)
1938	656	113	—
1947	2,409	350	252
1948	2,762	390	260
1949	2,967	417	258
1950	3,501	464	272

'The per capita real national income was about the same as in 1938'. In 1950 it 'exceeded the 1938 figure . . . It was primarily due to the high prices of exports.' Except for operations incidental to processing for export, there were, until recently, no local manufacturing industries of any significance.<sup>2</sup>

While 3,250,000 acres are cultivated today, it is estimated that an equal amount is available for cultivation.<sup>3</sup> The present man-land ratio is less than .5 acres per head. Even with the new land brought in, it would be less than 1 acre.<sup>4</sup>

Meanwhile the population is increasing at the rate of some 200,000 a year. Agriculture is the occupation of 60% of the population.<sup>5</sup> In 1935, incomes below Rs. 25 a month accounted for over 78% of the National Income.<sup>6</sup> The pre-war average rural family's monthly income was 'less than Rs. 20/- per month'. The 1950 average was Rs. 93/- 'from all sources'. Those depending on agriculture had an income of Rs. 95/-, those in handicraft Rs. 98/- and in trade Rs. 113/-, while the non-agricultural family had just Rs. 62/-.<sup>7</sup>

1. Economic and Social Development in Ceylon 1926-50 (A Survey)—presented to Parliament by the Hon. Minister of Finance. Table constructed from figures at para 86 of page 25 and table II of Appendix.

2. Ministers' Post-War Development Proposals—v. & The Colombo Plan.

3. The Colombo Plan, page 29.

4. cf. I.L.O. Report, page 22 and Sessional Paper 11 (Ceylon) of 1950, page 8.

5. Das Gupta, Economic Survey of Ceylon, page 30.

6. Das Gupta, page 29.

7. Sessional paper 11 of 1951, page 10. Prepared by the Dept. of Census and Statistics.



Under-employment clearly exists. Sub-division and fragmentation have gone on for a long time. The Pochkanawala Banking Commission Report was able to mention a holding  $1/138$  of an acre. The following Tables reflect the present state.<sup>1</sup>

Tenancy is also of considerable importance. The last census of Ceylon reckoned that holdings not fully owned amount to nearly 40% of the total.

Table

Asweddumized Paddy Lands (Exclusive of Paddy Lands within Estates) by districts, showing Number of holdings, Total Extent, and Average Size Ceylon, 1946.

District	Number of holdings	Total Extent	Average Size (Acres)
CEYLON	771,908	889,970	11/5
Colombo	68,097	62,567	09/10
Kalutara	30,790	46,132	11/2
Kandy	67,025	39,731	03/5
Matale	38,642	21,292	03/5
Nuwara Eliya	25,462	16,646	07/10
Galle	32,884	48,992	11/2
Matara	27,655	48,789	14/5
Hambantota	10,362	38,417	37/10
Jaffna	57,484	52,881	09/10
Mannar	9,044	23,356	23/5
Vavuniya	8,258	22,644	27/10
Batticaloa	17,291	119,170	69/10
Trincomalee	4,737	21,592	43/5
Kurunegala	118,149	125,348	11/10
Puttalam	7,833	7,983	1
Chilaw	10,584	14,336	12/5
Anuradhapura	126,630	95,877	04/5
Badulla	44,950	33,747	04/5
Ratnapura	31,778	33,541	11/10
Kegalle	34,253	26,930	04/5

Table 184 : The Census of Ceylon—General Report.

1. The Census of Ceylon—General Report.



Table

Proportion per cent. of Asweddumized Paddy Land holdings below one acre in extent to all Asweddumized Paddy Land holdings in each District, (Exclusive of Paddy Lands within Estates), Ceylon, 1946

District	Proportion Per Cent.	District	Proportion Per Cent.
Colombo	68.0	Anuradhapura	74.2
Kalutara	45.0	Badulla	76.9
Kandy	82.1		
Matale	85.3	Ratnapura	55.8
Nuwara Eliya	75.4	Kegalle	69.5
Galle	49.0		
Matara	37.3		
Hanbantota	25.5		
Jaffna	75.5		
Mannar	26.6		
Vavuniya	17.0		
Batticaloa	2.3		
Trincomalee	17.1		
Kurunegala	59.8		
Puttalam	68.9		
Chilaw	52.3		

Table 186 : The Census of Ceylon—General Report.

Cultivated Holdings. (Selected Villages).<sup>1</sup>

District	No. of families with land	Land in acres	Average
Puttalam	84	394 $\frac{3}{4}$	4 $\frac{2}{3}$
Kurunegala	1,289	9,074 $\frac{1}{2}$	7
Galle	543	1,801 $\frac{1}{4}$	5 $\frac{1}{3}$
Matara	290	1,187	4

1. cf. Report on Economic Surveys of Selected Villages, printed as Sessional Papers in Ceylon.



## Ownership of Land. (Selected Villages).

District	No. of families	No. of families with land
Puttalam ...	173	84
Kurunegala ...	2,051	1,289
Galle ...	1,249	543
Matara ...	649	290

The 'Preliminary Report on the Economic Survey of Rural Ceylon, 1950', found that more than  $\frac{1}{2}$  the male population and about  $\frac{1}{5}$ th the female were gainfully employed. This is reflected vis-a-vis the other sectors, also in the following table<sup>1</sup>. It was quick to add however that "this suggests a higher level of employment than is actually the case."

Table

## Proportion per cent. Unemployed of Total Population

	Per Cent.
Agriculture and Related Occupations ...	0.47
Fishermen, Hunters, trapping &c. ...	0.43
Workers in Mine and Quarry Occupations ...	1.96
Craftsmen and Production Process Workers ...	1.36
Workers in Transport and Communications ...	2.26
Trade and Finance ...	1.61
Public Administration and Defence ...	2.57
Professions and Liberal Acts ...	1.37
Sports and Entertainments ...	1.31
Personal Service ...	0.76
Miscellaneous ...	1.74

Table 161 : The Census of Ceylon—General Report.

1. The Census of Ceylon—General Report.



There is undoubtedly, a volume of involuntary idleness which could be usefully employed in subsidiary occupations. It has assigned the reason to an agriculture "associated with a multiplicity of holdings most of them of uneconomic size." Associated with it is the seasonal unemployment inherent in agriculture irrespective of the size of holdings.<sup>1</sup> The seasonal movements of labour that take place may be assumed to reflect both these features. As an example, in 1921, about 77,100 of the 97,500 cultivators, and 4,000 of the 43,000 owner cultivators sought employment as casual labourers—in other parts of the country, or in neighbouring plantations.

Land rents are estimated to vary from  $1/6$  to  $1/2$  the crop according to region and type of crop.<sup>2</sup> Indebtedness is an urgent problem for both tenant and owner farmers. The boutique-keeper is the farmer's creditor. The village fair is the villager's market par excellence. Between the boutique-keeper and the middleman at the fair, the villager does not get much of a chance. His produce is perishable, while theirs is relatively non perishable. From them the villager buys on credit and gets loans as well. They are more familiar with buying practices and market conditions than he is. In the result he is invariably forced to buy dear and sell cheap.<sup>3</sup> In the result, he has become a debtor.<sup>4</sup> On the average, about 73% of the rural population (pre-war) may be said to be in debt; about 90% of it is estimated to be for unproductive purposes.<sup>5</sup> The villager lives at the margin of existence. Once the slightest initial maladjustment takes place the rest follows. Thereafter debt and poor price both become causes one of the other.

1. Sessional paper 11 of 1951—page 9.

2. I. L. O. Op. cit. page 43.

3. Economic Surveys (Kurunegala District) 1940.

4. The following recordings may be of interest. Ceylon Daily News, July 1949. 'The coconut industry in Ceylon has been commented on as a sort of 'Processors' Paradise and Producers 'Purgatory', by the Commissioner of Co-operative Development in his recent administration report. The Commissioner points out the travails of the small-holder in the hands of the middleman, and expresses the fear that the coconut industry will become the happy hunting ground of all types of middlemen. A recent departmental survey has revealed the "alarming extent of indebtedness among coconut smallholders", some of whom were found to have entered into agreements to sell their coconuts to local dealers, in one case at Rs. 18 per thousand, and in another case Rs. 40 per thousand nuts, as against the current market price of Rs. 100-110 per thousand nuts. In another still more flagrant case, the owner of an acre of land fully planted in coconuts had raised a loan of Rs. 300 on the usufructuary mortgage of his holding. For over 4 years the mortgagee had helped himself to the crops which on a conservative estimate, had during the period fetched over Rs. 1,200—i.e. four times the amount of the loan.

5. I. L. O. Op. cit. page 37.



During the Depression of the thirties, legal machinery for Debt Conciliation and Land Redemption was introduced. As a result of these steps, the co-operative movement and the inflation of the War and Post-War years, the position has improved. The percentage of debt-free families in 1950 was 66.5 as against about 25 in 1936-8. In contrast also to the pre-war position the average family in 1950 saved Rs. 11/- per month. But large numbers of families were below the average and there were several "whose income was insufficient to square up expenditure". Thus even in 1950, although the average debt per family was only Rs. 73.69 or less than the average family monthly income of Rs. 93.26, the average debt per indebted family was Rs. 219.98.<sup>1</sup>

This may be further verified from the following data. To start with, 29% of the families had no land of their own, 35% had areas under one acre, 27% between 1 and 5 acres, and only 9% over 5 acres. In addition, communal pastures were very few. The average family owned only .34 bulls, .75 cows, .55 buffaloes, .15 goats, .01 pigs and .85 poultry.<sup>2</sup> So that, too much must not be read into the present small saving from income, or the reduction in debt. The fact remains that, as in India, the economic basis is still not conducive to preventing further indebtedness.

Of the total family expenditure, 67% is on Food 8% on clothing and 25% on a number of miscellaneous items.<sup>3</sup> Two things may be noted. One, the ratio of expenditure on food to the total is very large; before the War, it was even larger. Two, it means that the standard of living, as judged by expenditure on other items, is very low. These items include betel, arecanut and tobacco, liquor, house and rent, medicine, travelling, fuel and light, education, gifts and assistance, toilet and washing, recreation, rates and taxes, and ceremonial. Nor is this offset considerably by the fact that "generally the house is owned or is occupied free of rent" or that in "in regard to medicine and education he (the peasant) avails himself of the free state services provided".<sup>4</sup> Certainly these make the real income of the peasant larger than his money income. But consideration of the following information suffices

- 
1. Sessional paper 11 of 1951, page 13 and 11.
  2. Sessional paper 11 of 1951, page 13.
  3. Sessional Paper 11 of 1951, page 11.
  4. Sessional Paper 11 of 1951, pages 11 and 12.



to show the state of housing. In regard to education, apart from a mere knowledge of the 3Rs, where the medium of instruction may not be so relevant, any satisfactory education so far had been imparted only through the medium of English.

In taking the satisfying figures for literacy into consideration therefore, it is necessary to couple it with the figures for literacy in English. Education for most people thus stops in their early years, with a bare knowledge of the uses of their mother language, even this to become eventually only imperfectly remembered. The information, referred to, on education and housing, is annexed in the following tables.

In regard to medicine, the death rate of 12.9 per thousand in 1948-50 "compares favourably with rates obtainable in European countries." But shortage of trained personnel like doctors or nurses has been described as "one of the greatest drawbacks" and the general shortage of medical facilities is still being felt acutely."<sup>1</sup>

Floods and droughts have been two of the special economic risks in Ceylon. The general dearth of capital accentuates the problems. In the "Dry" Zones, in the northern portions of the country, the Government has undertaken extensive programmes of settlement and colonisation by restoring the ancient tanks. The recent Gal-Oya scheme in the Eastern Province is a more ambitious Multi-Purpose scheme.

Table\*

Percentage Distribution of Dwellings Classified According to the Material of Construction of Roof, for Urban and Rural Areas, Ceylon, 1946

Material of roof	Percentage distribution of dwellings	
	Urban (M.C.C. and U.C.C.)	Rural (Including Estates)
Thatch ... ..	26.1	68.0
Tile ... ..	67.3	22.9
Zinc ... ..	5.1	7.8
Asbestos ... ..	0.4	0.3
Shingle ... ..	0.1	0.1
Other ... ..	1.0	0.9

1. Economic and Social Review of Ceylon pages 3, 46 and 18.



Table†

Percentage Distribution of Dwellings Classified by the Number and Rooms for Urban and Rural Areas, Ceylon, 1946

Number of rooms in dwellings	Percentage distribution of dwellings	
	Urban M.C.C. and U.C.C.	Rural Including Estates
One ... ..	35.1	38.6
Two ... ..	32.0	35.7
Three ... ..	15.2	16.1
Four ... ..	7.5	5.5
Five ... ..	4.1	2.0
6-7 ... ..	3.8	1.2
8-9 ... ..	1.3	0.3
10-11 ... ..	0.5	0.3
12-13 ... ..	0.2	0.1
14-15 ... ..	0.1	—
16 and over ... ..	0.2	0.2

\* Table 175 : The Census of Ceylon—General Report.

† Table 176 : The Census of Ceylon—General Report.

Table 1\*

Percentage Distribution of Dwellings, Classified by Principal Material of Construction of Outer Walls, for Urban and Rural Areas, Ceylon, 1946

Material of outer walls	Percentage distribution of dwellings	
	Urban U.C.C. and M.C.C.	Rural Including Estates
Cadjan ... ..	5.6	5.5
Mud ... ..	29.1	71.0
Wood ... ..	1.6	1.0
Zinc ... ..	0.9	0.1
Stone ... ..	10.8	12.7
Brick ... ..	48.7	8.2
Concrete ... ..	1.4	1.1
Other ... ..	1.9	0.4



Table 2†

Percentage of Literates in Ceylon Relative to Population Aged Five Years and Over, 1881-1946

Population—	Persons Per Cent.	Males Per Cent.	Females Per Cent.
(aged 5 years & over)	100.0	100.0	100.0
1881	17.4	29.8	3.1
1891	21.7	36.1	5.3
1901	26.4	42.0	8.5
1911	31.0	47.2	12.5
1921	39.9	56.4	21.2
1946	57.8	70.1	43.8

\* Table 174 : The Census of Ceylon—General Report.

† Table 123 : The Census of Ceylon—General Report.

Table

Percentage of Literates in English to the Total Population, by sex, in each District (Excluding Children, Aged 0-4 Years) 1946 and 1921

District	1946			1921		
	Persons	Males	Females	Persons	Males	Females
Colombo ...	13.3	16.5	9.3	8.2	10.7	5.3
Kalutara ...	5.0	7.1	2.9	2.8	4.2	1.3
Kandy ...	6.3	8.4	3.9	4.3	6.0	2.4
Matale ...	4.4	5.9	2.8	2.7	3.7	1.3
Nuwara Eliya	3.7	5.2	2.0	3.2	4.4	1.8
Galle ...	5.7	7.9	3.6	3.3	5.1	1.6
Matara ...	3.2	4.3	2.2	1.8	2.5	1.1
Hambantota	1.8	2.5	0.9	1.0	1.3	0.4
Jaffna ...	9.1	12.4	5.7	4.1	6.7	1.6
Mannar ...	3.6	4.6	1.9	1.7	2.5	0.6
Vavuniya ...	3.8	5.5	1.3	1.7	2.6	0.5
Batticaloa ...	2.7	3.6	1.7	1.7	2.5	0.8



Trincomalee	11.4	14.9	3.9	4.2	5.9	2.1
Kurunegala	1.9	2.7	0.9	1.0	1.5	0.5
Puttalam ...	2.5	3.5	1.1	2.0	2.5	1.1
Chilaw ...	3.2	4.1	2.2	2.2	3.1	1.3
Anuradhapura	2.7	3.8	1.1	1.6	2.3	0.5
Badulla ...	3.5	4.9	1.8	2.1	3.0	1.1
Ratnapura	2.7	3.8	1.5	1.8	2.7	0.7
Kegalla ...	2.4	3.4	1.3	1.6	2.3	0.6

Table 126 : The Census of Ceylon—General Report.

In every aspect of rural activity, the Co-operative movement, as in India, has proved its worth. In regard to Debt, "of the many measures taken to combat it the path of co-operation has been the most fruitful".<sup>1</sup>

Defective marketing is a feature that could be inferred from the foregoing descriptions of rural life. The following instance may be an indication of what could be expected from a more efficient system. When the Government bought certain specified products in unlimited quantities at guaranteed minimum prices, the output of onions (which was among the specified products) in Jaffna is calculated to have risen in one year from 100 tons per year to 2,000 tons per year.<sup>2</sup>

### The Plantations

As already mentioned, fluctuations in prices of the plantation products cause serious dislocations to the economy. The experience recently of one of the largest changes in prices known to the rubber industry is an outstanding example. From the abysmal level of only some months previously it registered record 'highs'. In the past, there have been serious and disconcerting movements in prices, with increased output often securing smaller total revenue. The following three tables,<sup>3</sup> for Tea, Rubber and Coconut, respectively, are worth setting down in full.

1. Sessional paper 11 of 1951, page 13.

2. Sessional paper 11 of 1950, page 10.

3. Ministers' Post-War Development Proposals, pages 3, 4, and 5.



## TEA

Year	Quantity Million lb.	Price per lb. Rs. cts.	Value Rs. Million
1924	205	1.04	215
1925	210	0.96	200
1926	217	0.99	213
1927	227	0.94	214
1928	237	0.85	201
1929	252	0.81	205
1930	243	0.75	182
1931	244	0.57	139
1932	253	0.42	108
1933	216	0.54	118
1934	219	0.66	145
1935	212	0.64	146
1936	218	0.67	153
1937	214	0.76	171
1938	236	0.70	172
1939	228	0.77	188
1940	246	0.82	208
1941	238	0.92	255
1942	266	1.02	254
1943	264	0.92	269
1944	276	1.05	311
1945	232	1.13	278

## RUBBER

Year	Quantity Million lb.	Price per lb. Rs. cts.	Value Rs. Million
1924	83	0.75	64
1925	102	1.73	170
1926	132	1.21	170
1927	125	0.95	119
1928	128	0.55	74
1929	181	0.52	87
1930	171	0.27	47
1931	138	0.14	20
1932	111	0.11	13



Year	Quantity Million lb.	Price per lb. Rs. cts.	Value Rs Million
1933	142	0.15	23
1934	179	0.31	57
1935	120	0.30	38
1936	112	0.41	47
1937	156	0.50	77
1938	115	0.37	45
1939	135	0.47	68
1940	197	0.55	113
1941	202	0.56	118
1942	251	0.66	172
1943	220	0.71	169
1944	224	0.98	223
1945	224	0.96	218

## COCONUT

Year	Quantity Million Nuts	Price per 1,000 Rs. cts.	Value Rs. 000
1924	29	85.82	2,499
1925	23	83.33	1,941
1926	17	82.22	1,394
1927	19	80.27	1,515
1928	18	79.06	1,424
1929	21	60.07	1,282
1930	21	46.58	972
1931	21	37.12	759
1932	23	44.60	1,136
1933	22	29.36	578
1934	31	19.42	608
1935	21	35.71	1,111
1936	17	43.03	916
1937	11	45.17	621
1938	16	26.56	635
1939	12	34.34	518
1940	7	39.91	228



Year	Quantity Million Nuts	Price per 1,000 Rs. cts.	Value Rs. 000
1941	7	25.43	279
1942	5	46.54	150
1943	20	67.60	684
1944	24	72.50	1,251
1945	29	85.25	2,207

The following Table<sup>1</sup> illustrates the fluctuations in output on the farm (or estate).

### FARM OUTPUT

Products	Average Output	Fluctuations
Tea	350 lbs per acre per year	250—650 lbs.
Rubber	300 " " " "	200—600 lbs.
Coconut	1,500 nuts " " "	1,500—4,000 nuts.
Paddy	20 bushels per acre per crop	15—60 bushels.

### Secondary and Tertiary Sectors

On industries, in the words of a recent survey, 'there is not much to say'. Before 1939, there were one cotton mill, a couple of match factories, distilleries, and some public works and engineering works.<sup>2</sup> The cotton mill produced in 1947, 1.5 million pounds of yarn and 3.1 million yards of cloth. In cottage industry there are estimated to be 8,000 looms with a producing capacity (post war) of 10 million yards. The amount of clothing imported in 1938 was about 70 million yards. Of the Government factories, at least four had still shown losses at September 1945. The items covered by the factories were plywood, steel rolling, coir, paper, leather, quinine, glass, ceramics, acetic acid, saw mill, industries workshop, and carpentry workshop. All these, except for coir which was started in 1939, dated from 1941 and after. New

1. Sessional Paper 11 of 1950, page 42.

2. Gupta. Op. cit. page 43.



industries and increase in output of existing ones contemplated, covered cement, glass, plywood, steel, paper, caustic soda, hydrogenated vegetable oil, sugar and textiles.<sup>1</sup> Plumbago is the most important mineral. A large hydro-electric scheme is in course of construction.

The foregoing gives an idea of the types of resources available. In most cases, however, the supplies are extremely limited. Cement and ilmenite are two of the exceptions. It is well however to count among the potential resources the scope for fishing and salt manufacture and the suitability of large extents of land for cotton and sugar.

The areas per mile of railroad and highway, are, relatively speaking, satisfactory. The figures (1947) are 27.7 square miles and 3.9 square miles. The distribution of the mileage over the country is uneven. Most of the railway mileage is in the plantation areas, as are also the better part of the highways. In the North Western, North Central and Eastern portions of the country it is very easy to come across villages and areas with extremely imperfect or no means of communication.

The total capital invested, of which 85% was foreign, is estimated at 1947 market values at Rs. 1,335 million; private savings at Rs. 2 million a year; rupee savings by companies at Rs. 6 to 10 million; and savings from Insurance at about Rs. 3 million. Government Loan expenditure in 1947-8 was Rs. 116.1 million as against 'Revenue' expenditure of 435.7 million. The State utilised 27% of the National Income. Most of its expenditure is on Social and Utility Services, with development schemes coming a distant second. It may be noted that in 1948-9, 66.7% of Tax Revenue came from indirect sources, chiefly Import and Export duties.

The credit system does not extend far beyond the Exchange banks in Colombo. Some of them have branches in the country. Their business is confined almost entirely however to exchange business and provision of working capital to the Plantations. The Bank of Ceylon has reached a wider field, both in harnessing

---

1. Budget Speech, '48-9.



savings and in lending to different sections of the economy. But much more progress remains to be made. Besides, the problem of long term finance, agricultural and industrial, still exists. State finance was organised through the State Mortgage Bank and the Agricultural and Industrial Credit Corporation. They have yet to come up to the expectations held at the time of their establishment. The establishment of the Reserve Bank in 1950 is however bound to produce tangible changes in the entire credit structure.

### Foreign Trade

The foreign trade of the country, as stated, is subject to great fluctuations in value. It is also greatly limited in value, from the point of view of the standard of living. The terms of trade, compared to the position in 1938-9, were conspicuously adverse from 1942 until 1950.<sup>1</sup> The change, thereafter, for the better again seems to be temporary. In 1939, rice imports of 10,400,000 cwts cost Rs. 54 million ; in 1947, 5,000,000 cwts cost Rs. 134 million. The recent high prices for rubber helped to protect the finances. It does not represent however, a normal position. Nor, of course, do the War years. The essential point is that the earnings from exports have never been adequate to enable imports large enough to create a satisfactory standard of living.<sup>2</sup> The following table<sup>3</sup> gives a fair idea of the pattern of Ceylon's trade. It is of interest also to the points we take up in a later chapter.

---

1. Ministers' Post-War Development Proposals, page 26.

2. c.f. also Rita Hinden—"It is usual, in rapidly developing 'young' countries, to find that a good share of the import trade is concerned with the purchase of capital goods—machinery, transport vehicles, and equipment, perhaps raw materials for manufacture, building materials, and so on. A high proportion of such capital goods signifies a rapid rate of progress, and is regarded as a healthy symptom. In Egypt, for example, in 1936, producers' equipment, of one sort or another, accounted for as much as 75% of the imports; in Australia for 71%; and in New Zealand for 62%." The proportion of wholly or mainly manufactured imports to Ceylon in 1947 and 48 were 37% and 36%. The proportion of capital goods is bound to have been even smaller.

3. Gupta—page 92.



## Trade Distribution (Rs. Million).

	1939		1946		1947	
	Import	Export	Import	Export	Import	Export
U.K. ...	46	151	115	401	176	299
Rest of Sterling Area	112	46	343	171	440	220
Canada and Newfoundland	1	13	19	13	65	49
U.S.A.	6	63	42	90	112	121
Rest of America (excludes Argentine & Brazil)	0.8	2	4	4	7	16
Rest of Europe	16	22	8	17	40	40
Switzerland	0.5	0.4	5	2	4	3
Rest of World	61	12	162	33	135	67
Total	243.3	309.4	694.4	731	979	815

In the pre-war period there was, save in 1932, a favourable balance on Merchandise account. The following Table<sup>1</sup> shows the position up to 1947. The adverse balance on current account changed in 1950, only to become adverse again towards the end of 1951. The composition of the invisible items and the capital imports required for development, make it necessary that development must be carefully co-ordinated and priorities carefully arranged.

Balance of Payments (Current Account)  
(Rs. Million)

Class	Credit Movements				Debit Movements			
	1938	1945	1946	1947	1938	1945	1946	1947
1. Merchandise	289	666	765	889	234	608	684	972
2. Interest & Dividends	9	26	31	25	56	103	142	115
3. Other Services	17	445	164	55	52	112	82	78
4. Gold Coin & Bullion	—	—	—	—	—	—	—	8
	+315	+1137	+960	969	342	823	908	1173
	-342	-823	-908	+1173				
Balance on Current a/c.	-27	+314	+52	-204				

1. Gupta—page 94.



A brief reference to the inter-war depression of the thirties, as it affected Ceylon, will not be out of place here. The reaction of the economy to the slump may be noted under two heads. In the first place, "the majority of the people have a subsistence economy, that is, they produce mainly for their own consumption."<sup>1</sup>

The data earlier set down explain the nature of the rural family budgets, the very small expenditure on luxuries and the insignificant sums spent on housing and the like. A depression, in the sense generally understood, tends, so to speak, to pass over their heads and leave their positions almost untouched. Any adverse effect of a slump on the meagre medical or allied services in rural areas may be considered to have been counterbalanced by the relief schemes organised in the thirties by the Government.

The other side to the economy is, of course, the export sector and those directly dependent on this. It was in the export sector that the depression was most felt. The figures given on pages 128 and 129 above testify amply to the plight of the plantation industries in the slump. The following figures also confirm that the only mineral industry, plumbago, was in the same plight.<sup>2</sup>

Commodity Unit	1943	1944	1945	1946	1947	Average
	Rs.	Rs.	Rs.	Rs.	Rs.	1931-47
Plumbago F.O.B.						
Per Cwt.	25.99	23.98	22.75	21.78	20.04	13.74

The following figures<sup>3</sup> for Total Trade on Merchandise account (1926-1940) show that the lowest balances (which include an adverse balance in one year) were between the years 1928 and 1935, and that the figure did not return to the 1926 level till 1940 (vide the following Table 1).

- 
1. Economic and Social Development of Ceylon, 1926-50, page 25.
  2. Ibid from Table XIII.
  3. Ibid from Table V.



Table 1

## Total Trade—Merchandise

Year	Rs. million			
	Imports	Exports	Total Trade	Balance of Trade
1928	400	418	818	+ 18
1929	403	423	826	+ 20
1930	302	323	625	+ 21
1931	218	233	451	+ 15
1932	196	189	385	— 7
1933	177	200	377	+ 23
1934	217	264	481	+ 47
1935	228	253	481	+ 25
1936	214	268	482	+ 54
1937	243	332	575	+ 89
1938	236	285	521	+ 49
1939	242	328	570	+ 86
1940	283	387	670	+ 104
1941	287	424	711	+ 137

Table 2

## Revenue, Expenditure and Loan Fund Expenditure

	Revenue (Rs. million)	Expenditure (Rs. million)	Loan Fund Expenditure (Rs. million)
1925-26	124.5	110.0	5.9
1926-27	129.4	121.0	3.1
1927-28	134.1	152.1	.3
1928-29	107.8	125.9	.2
1929-30	110.9	110.3	12.6
1930-31	101.8	100.3	4.8
1931-32	84.8	96.9	3.0
1932-33	106.1	92.7	1.6
1933-34	104.1	93.4	1.1



	Revenue (Rs. million)	Expenditure (Rs. million)	Loan Fund Expenditure (Rs. million)
1934-35	99.0	107.3	1.9
1935-36	102.8	109.5	2.2
1936-37	119.2	108.8	2.9
1937-38	113.3	115.3	5.1
1938-39	116.9	127.1	7.6
1939-40	132.7	122.4	6.5
1940-41	135.5	127.3	5.4
1941-42	158.8	153.3	23.7
1942-43	200.0	185.0	26.1
1943-44	250.6	210.7	27.7
1944-45	303.9	254.4	31.6
1945-46	383.3	312.9	36.0
1946-47	461.2	405.4	32.1

Government finance was linked heavily, through the import duties (over 60% of budgetted revenue during these years) and the income tax, with the fortunes of world trade and other export industries. The result is reflected in the previous figures<sup>1</sup> of Revenue, Expenditure and Loan Fund Expenditure for the years 1925-6 to 1946. (Table 2 : vide last page). The depression had been wrought by world economic conditions. Nothing could be done, in the short run, to fight it successfully. Devaluation, for instance, would have done little—in Ceylon—to alter the effects. It would only have increased the prices of the consumption goods which were being imported, and whose demand was relatively inelastic. By cheapening the purchase price of exports, it would not have thereby increased sales sufficiently to make an appreciable impression on the economy. The Restriction Schemes were more successful instruments of policy, though even their contribution was mainly to prevent further deterioration in the conditions of the countries concerned. It is fairly evident that financial practices or policy, to further the objective of full employment,

1. Ibid from Table XXI.



would not have succeeded in the existing economic background. Structural development was called for. It was a long term, but the only, solution.

### **Capacity of the Existing Economy**

The capacity of the present export industries, in relation to full employment needs, may now be assessed. The question may be put as one of producing more tea and rubber as against more rice and fish or clothing and shoes.

The case, for or against, may normally be illustrated by the familiar production-possibility ratios, or the curves derived therefrom. Ceylon could produce clothing and shoes, but 'at a cost'. It is cheaper, so would run the argument, to produce tea and rubber (T for short) and 'transform' it into clothing and shoes ('C') by importing the latter, because the number of units of T sacrificed in producing C internally, is more than the number needed to import the amount. In other words, a given amount of effort in producing T will earn more C abroad than can be produced at home. Any ratio in trade that is more favourable than that in internal production justifies continued reliance on T. If, for instance, a given amount of effort produces internally either 10 units of T or 5 of C, a ratio that is above this is sound basis for trade. But the type of economic policy we have advocated in this Book is based on development in lines other than T. The implication would be that a ratio between T and C that justified trade will cease to exist if we place continued reliance on T for fulfilment of 'full employment' needs. Even for maintenance of present economic levels, some adjustment of the structure may be called for on examination of the production possibilities. Let us consider the relevant factors.

Statistics of production and price for the plantation industries appear to indicate conclusively that the fluctuations were far more in price and income than in volume of output.

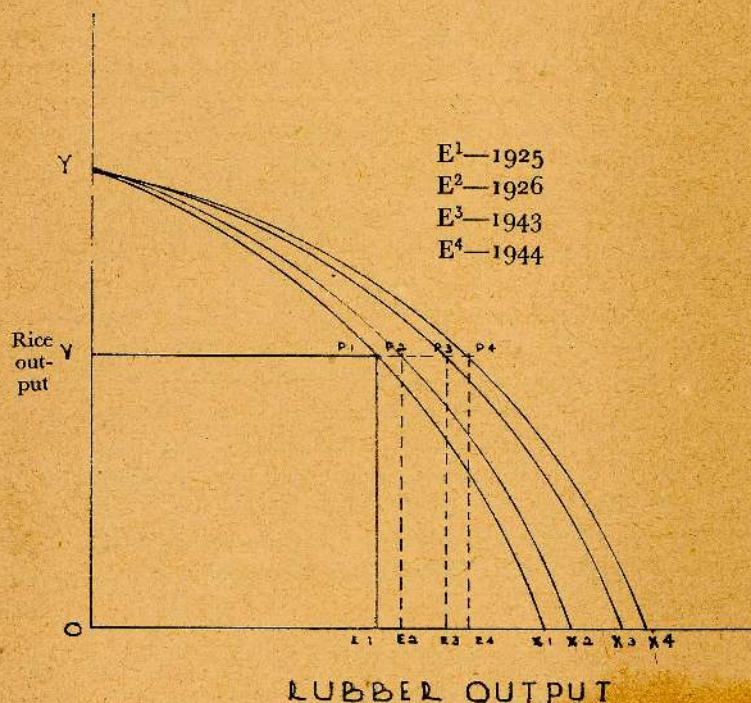


It meant that juggling with quantity of output was apparently futile to ensure a desired level of income. External depression or buoyancy seems to have determined the price. It was not possible to cut output for a higher price, partly because of the conditions of agricultural production and mainly because prosperity or slump in the industrial countries was the chief determinant of the terms of trade. An increase in output, therefore, would secure higher incomes only assuming boom conditions in the buying countries. Alternatively, one must assume a vast extension of buying countries in the world. The production possibilities for the plantation industries may then be assessed partly by experience of the past and partly by the tendencies for the future. In practice, past experience would determine any possibilities of achieving full employment through these industries in a relatively short term; future tendencies are more useful as a study of the long-term ultimate possibilities.

Taking the short term, we may consider the figures of Production, Price and Value for Tea, Rubber and Coconut, given in pages 128 and 129 above. The following observations may immediately be made. The total revenue on Tea ranged from Rs. 108 million in 1932 to Rs. 311 million in 1944. For Rubber and Coconut, the range was far more spectacular. In the latter, it was from Rs. 150,000 in 1942, to Rs. 2½ million in 1924; in Rubber, it was from Rs. 13 million in 1932 to Rs. 223 million in 1944.

If revenues in 1950 or 1951 are considered, the ranges become even wider. As it is, the 'maxima' figures for Rubber and Coconut are about twenty times the 'minima'. For the next observation we make we may, for convenience, confine ourselves to Rubber. In the years 1925, 1926, 1942 and 1943, the figures of output (in million lbs.) were respectively 102, 132, 251 and 220. In all these years, however, the total revenue remained the same at Rs. 170 millions. Similar evidence can be picked for other years. We may depict this through production—possibility curves, taking rice and rubber as the two competing types of output.





Suppose given allocations of resources produced  $OV$  of Rice and  $OE^1$  of Rubber in 1925. Since the plantation industries were mostly worked by immigrant Indian labour which adjusted its numbers by voluntary repatriation in times of slump we may for convenience assume the output of rice to have been unaffected by increases in rubber production. Looking at the diagram one gets the impression that spectacular additions to the national income were recorded by Rubber. But  $E^1$ ,  $E^2$ ,  $E^3$ , and  $E^4$  are widely varying levels of output for which the contribution to the National Income was in all cases the same. If the  $OX$  axis represented imports into which the Rubber output was 'transformed',  $E^2$ ,  $E^3$  and  $E^4$  should all be at  $E^1$ . Of course if  $E^3$  or  $E^4$  could have been sold at prices fetched by  $E^1$  or  $E^2$ , an enormous revenue would have accrued. But there is little evidence to support the conjecture



that prices in 1925, '26 would have remained the same if output had risen to the levels shown by  $E^3$ ,  $E^4$ . Nor does it show that output in 1942 or '43 should have been reduced, till price rose sufficiently to net a larger revenue. Only in 1944, a slightly larger output than  $E^3$  secured the maximum revenue among the years shown in the table referred to. But for purposes of achieving full employment and of raising the standard of living, it will be mistaken to push along on the OX axis ; it may be more wise to go up on the OY axis. It may be noted that  $E^4$  represents the highest output figure in the table mentioned, and  $E^1$  one but the lowest in the series.

The real question for rubber is, Round what point, say between  $E^1$  and  $E^4$  should production be controlled. If output is 'permanently' at  $E^1$  large sums of revenue would be lost in times of high price; it would take too long to expand output sufficiently to take advantage of the high price. If output was maintained at  $E^4$  it would have been justifiable if 1943 or 1950 prices represented the more likely levels. But at 1942 prices, the country would have been in a better position if the resources producing output between  $E^1$  and  $E^4$  had been already employed to increase output along OY.

Maintaining output at  $E^4$  can be defended if, under falling prices, resources can be immediately switched over to more rice production. But this degree of non-specificity in factors cannot be had even for rice farming, much less for a diversified program of development. The obvious course is to have an output, not so much behind  $E^4$  that it cannot expand fast enough to make fair use of rising prices, and not too ahead of  $E^1$  to be saddled with gluts or idle resources in times of slump. Of course,  $E^4$  is assumed to be a maximum point, under given conditions of physical capacity of world demand ; so also is any point selected between  $E^4$  and  $E^4$  for purposes of maintaining average production. A secular expansion in world economy, new uses for rubber, or new areas of demand will alter these points radically. But the principles, on which to determine average production, must remain the same.

On short-term possibilities, the terms of trade also throw some light. A calculation of the terms is itself based on a base period, which may exaggerate the difference in relative prices, over the



years, or minimise it. They are a useful index, however, of the relative strengths in the 'pulls' of export and import goods. In this light, it would not be difficult to read the necessary implications. The terms are also influenced by the presence or otherwise of a diversified economy at home. Production possibilities could be considerably different if that assumption were allowed for.

For the present, we may look at the data as they exist. The following Table<sup>1</sup> gives the prices of Raw materials and Manufactured Articles from 1929-38 with the indices at 100 in 1929. The downward trend in prices reflecting the great depression exists in both categories, but it is noteworthy that in no year were raw material prices equal to or above industrial prices.

### Movement of Prices in International Trade

(1929—100)

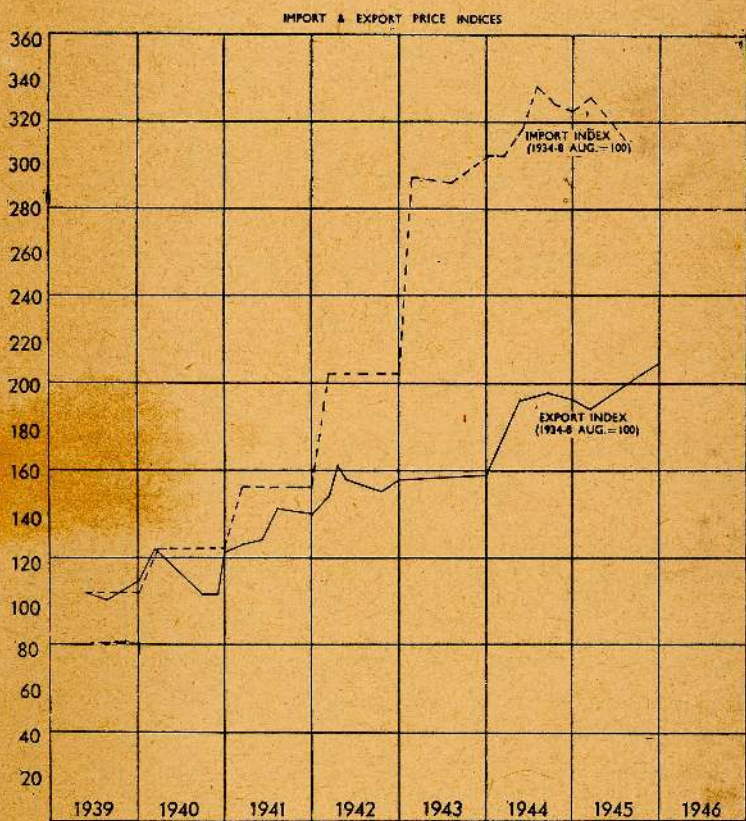
	1929	30	31	32	33	34	35	36	37	38
Raw Materials	100	82	59	44	40	39.5	39	41.5	47	42.5
Man. Articles	100	94	78	63.5	56.5	50	48	48	51	50.5

The following chart<sup>2</sup> gives the import and export price indices for Ceylon during 1939-46 with the average for 1934-38 as 100. (It is likely that 1929 as base year may depict the position in a worse light.) These years were generally ones of 'maximum' production. The results are still not quite favourable. It is true they were War years and, therefore, import prices were bound to be high. The data of these years, however, are useful to water down any optimism that may arise over a new re-armament drive and feverish demand for raw materials. Such a situation generally cuts both ways, since import goods also become in short supply. If past data indicates anything, it is the industrial countries that retain, in the end, the better bargaining power. In the circumstances, the more adverse the terms of trade become, the less advantageous it becomes to stick to the existing lines of production.

1. Ghate. *Asia's Trade* page 30.

2. Ministers' Post-War Development Proposals.







Beyond a point, it is not worthwhile importing certain goods since they could possibly be made at home at something like the import price. The data, referred to above, suggest that in certain years such a possibility existed. The institution of several factories by the Ceylon Government during the war was largely enabled by this feature. Clothing and shoes were two prominent cases. This adverse gap between the import and export prices does not however prove finally a case for industrialisation, since such larger gaps as may have justified the policy were never permanent. They were all part of the cyclical movements in world economic activity. In that sense, there is only enough argument for a relatively small degree of diversification to give a better bargaining power and to check the more serious effects of trade fluctuations. Even within the existing framework, the production possibility argument recognises that a little of the best land in an industrial country will hold its own in food production and a little industry (probably cottage crafts) in the agricultural country would be sufficiently low cost to continue in production. So that there is no grave ideological conflict about development in this limited sense.

We may therefore turn to the long-term possibilities. The point we now have to consider stems from the fact that the terms of trade, narrowly conceived, are not everything. Our enquiry is into the capacity of the plantation industries to secure full employment; not into mere anti-cyclical policy. Certain vital points emerge. The National Income of Ceylon, in relation to the income required for full employment, is only a minor fraction. The exact figure depends on the standard of living attached to the term full employment. On English standards, the present Income of Ceylon is  $1/10$  and on U.S. standards  $1/20$  of the requisite income.<sup>1</sup> Even if it is not fair to take either of these as a standard of reference, it is clear that the present national income is only a minor fraction of the income required for full employment. Let us take a five-fold ultimate increase of income as reasonable. Of the present national income, the contribution of the plantation industries does form a handsome proportion, roughly half. The capacity of these industries in relation to full employment needs may be interpreted in two ways. If they are to be solely responsible

---

1. Vide page 108 above and f.n. 7 therein.



for further increases in national income their output (given the terms of trade) will have to multiply nearly ten-fold. Alternatively, we may suppose that other sectors like rice, handicrafts, and so on will still constitute half the total income. In that case, the 'plantation' output must increase five-fold. A glance at the production figures of the past will show that the variations in output so far were scratches on the surface compared to what is demanded. The new target is so great that it ceases to be a matter of degree.

Three questions may now be answered. Can that new output be produced? Can it be produced at costs low enough to meet effective demand? Will it be within physical consumption limits? In Ceylon, it is fair to say that all the really suitable land for tea and rubber is practically used up. The terrain, the climate and the rainfall that tea and rubber require are confined to the areas where these already grow. Coconut can still expand, extensively and intensively, in certain areas. Yet it is highly doubtful if output could increase more than two-fold.<sup>1</sup> The question of costs follows partly from this. An established industry of this type normally operates under increasing costs.<sup>2</sup> In any case, the contemplated increase in output certainly involves rapidly increasing costs. Besides, existing costs themselves may be too high for the future. The cost trends for synthetic rubber, success on a better groundnut scheme, these mean that even on existing output the need for cost-reductions must be considered sooner or later. Tea-drinking is a habit. Habits, like fixed exchanges under the gold standard, have always been a solace and encouragement to merchant-exporters; they are taken for granted and expected to last. But even as they develop imperceptibly they could die off slowly. The change may be 'social' but could be aided and abetted by the economic climate. It would not be wrong to presume that under pressure of an upward rising cost curve our consumers abroad would begin to change, and after some time like it too! Further, the whole case for stepping up tea production is based on new consumer markets being developed. New markets are not likely to be won under increasing cost conditions. The

---

1. The same roughly goes for increase in rubber through introduction of high yielding trees as in Indonesia, Malaya.

2. Though, set-off partly, by the higher yield of the better trees introduced.



unhelpfulness of past price indices in trade is greatest in this connection. It is theoretically possible that world demand in the future will increase sufficiently to absorb a five-fold increase in 'plantation' output ; if the habit of tea-drinking wins over those of beer and wine consumption; if, 'ground-nuts' continue to fail; and if new industrial demands in developing countries outstrip all supply in rubber, natural and synthetic.<sup>1</sup>

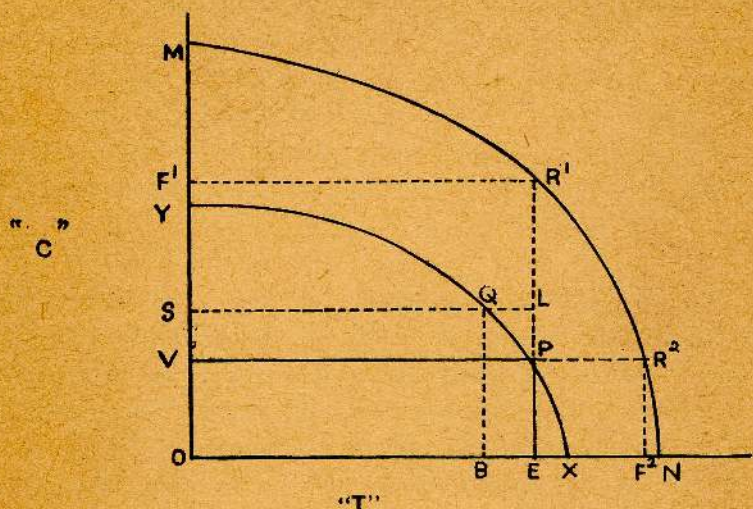
But these possibilities would appear too conjectural for formulating policy. New demand for rubber means extensive industrialisation in several agricultural countries. To assume the latter is, in the present context, to beg the question. The future of industrialisation and that of plantation produce seem far more closely and directly correlated than is assumed. They do not seem alternatives but 'complementaries'. If plantation produce were expanded, the safer forecast would be one of a discrepancy between supply and demand so large, and an adverse turn in the terms of trade so considerable, that the effort put into producing the extra tea and rubber would be more wisely put into producing 'clothing and shoes' at home. This is strengthened by the infant industry, or, as we stated earlier, the infant economy argument. This argument implies that new units will generally operate under decreasing cost conditions. The early high cost, should, despite initial teething troubles, tend to decline. It is the argument built round fixed factors and indivisibilities and is one generally accepted in qualifying production-possibility ratios. This tendency is in contrast to the opposite tendency in the existing industries. It, thus, hastens the stage when production of clothing and shoes would be more economical than export of 'extra' tea and rubber.

If we simplify the problems somewhat, the position may be illustrated thus.

---

1. c.f. China's new demand from Ceylon. If so, Ceylon would do well to raise high yielding trees which should be able to double her annual output.





The curve YQPX may be assumed to state production-possibilities in Ceylon at the moment. The present quantum of employed resources could produce OX quantities of T or OY of C. C may be considered to include all items not covered by T, though exclude the tertiary sector. This inclusion is in keeping with our descriptions earlier, and subsequently, of the "industrialisation" contemplated.

Suppose present production is OE of T and OV of C. Increase in production of C, by VS, is at the expense of T (to the extent of EB) only if we assume the total quantum of resources to be employed to remain the same. But we have seen earlier that the country has considerable unused natural and human resources. Economic development by increase in production of C to OS will, therefore still leave untouched the output OE, of T. The existing production-possibility curve is irrelevant as it cannot pass through point L. The new curve will be one of which point L is a part.

Alternatively, an increase in production of T may be achieved, with the unused resources leaving output of C at OV. But, we noted earlier the ultimate benefit of decreasing costs in C and the likelihood of increasing costs and adverse terms of trade in T. The chances are that the increase in T will not be more than the amount represented by VS for C. Further, beyond a point, the



ratio at which T and C are equated must be so altered that increases in T may no longer be real increases if 'transformed' into a common unit. T, unlike the 'domestic' and 'import-substituting' goods, has to be transformed in trade into general utilities 'G' before it can be considered an addition to the volume of G (or the National Income). Suppose for instance, the original price, on which the increase in production from OE to say  $OF^2$  was made, is suddenly halved. The National Income would in fact be *lessened*. In a sense, this is not an extreme example, if we grant anything like the enormous increases in T that we earlier postulated for full employment. The things to be compared are, beyond a point, not the effort expended in producing C at home as against that spent abroad, but the effort spent in producing C at home as against the effort needed to convert the *extra* T<sup>s</sup> into G.

If all the new resources (save those going into the tertiary sector) planned to be utilised under 'full employment' were utilised on C to produce  $OF^1$  units of C, the production pattern would be  $OF^1$  of C and OE of T. If the resources were utilised further in T, the pattern would be OV of C and  $OF^2$  of T.  $VF^1$  must be considerably greater than  $EF^2$ ,<sup>2</sup> even as VS must be less than EB. The actual pattern may be somewhere between the extremes  $OF^1$  and  $OF^2$ .<sup>2</sup> The very dynamics of the situation prevent any reasonable forecast.

It is known that general economic development in all countries is likely to step up demand for raw materials very greatly. But, the process is through 'industrialisation' and the attendant higher incomes all round. A reliance on past terms of trade, to read into future possibilities, demands a gratuitous assumption of full employment of men and resources. The production of 'clothing and shoes' is not at the expense of existing 'tea and rubber' production. When the production-possibility argument argues in terms of 'one at the expense of the other', full employment is presumed. The question for us is whether the unused resources should go even further into tea and rubber or into clothing and shoes. The nature of the change called for, and its extent, as well as the attendant uncertainties referred to, belong to a dynamic situation.



In that world, the production-possibility technique becomes nearly rudderless.<sup>1</sup>

The following sets of figures<sup>2</sup> for cereals tell their own story regarding the urgency of the economic problem for the country.

	1871	1881	1891	1901
A. Population	2,405,287	2,763,984	3,008,466	3,565,954
B. Paddy acreage	777,622	553,192	563,421	670,433
C. Quantity of rice imported in bushels	4,383,227	5,943,578	7,051,432	8,951,650
D. Bushels per head imported	1.82	2.15	2.36	2.36
	1911	1921	1931	1941
A. Population	4,106,350	4,497,854	5,306,871	6,633,617
B. Paddy acreage	644,763	798,514	850,000	912,500
C. Quantity of rice imported in bushels	11,569,809	10,254,925	15,281,959	8,879,435*
D. Bushels per head imported	2.82	2.28	2.88	1.34

\*. Owing to a world shortage of rice Ceylon could not obtain her full requirements of rice and this figure does not reflect the normal consumption requirements.

#### Supplies of Cereals in Ceylon<sup>3</sup> '000 tons

	1938	1939	1944	1945	1946	1947	1948	1949
1. Imports of Rice	522	584	112	179	254	258	409	397
2. Imports of Wheat flour	16	19	296	220	213	293	169	157
3. Imports of other grains of flour	24	31	47	65	35	65	19	158
4. Total imports of cereals	562	634	455	464	502	616	597	712
5. Home produce rice available for cons.	200	200	152	121	127	129		171
6. Total supplies (a)	762	834	650	636	612	843	827	959
7. Pop. on 1st Jan. (millions)	5.78	5.86	6.20	6.38	6.60	6.78	6.98	7.19

1. c.f. Remarks of W. A. Lewis quoted in pages 86—87 above.

2. Sess. paper 11 of 1950, Page 54.

3. Compiled from Official Ceylon Govt. sources, through courtesy of Ceylon Trade Commissioner's Office in London.



- (a) Excludes some 18,000 tons of cereals, other than rice, produced annually in Ceylon.

By 1921 apparently, the attraction of population to other sectors seems to have ceased. Openings for employment seem to have been sought increasingly in land again. The heyday of expansion in the plantation industries and the attendant tertiary sectors was at least over.

In the second Table a strict relation exists between items 7 and 6 in the long run. But the relation is established through imports (item 4) not home production (item 5). The latter figures are evidently vague, as accurate censuses were unobtainable. It was generally felt that considerable supplies existed which were not 'available for consumption.' The 'curve' for internal production may probably have been slightly upward; it may be fair at least to presume it to be a horizontal line, and not downward running as suggested by the figures in the Table. The phenomenal increases under items 2 and 3 were largely because further imports of rice were practically impossible. With this high-pressure demand on rice imports and the population increase, the consequences for the terms of trade are evident.

Significant extensions in acreage for rice cultivation have yet to be registered, as also reforms in size of holdings, in capital equipment and methods of cultivation. These are the 'initial major barriers'. The stagnation in internal output should not therefore surprise.

The 'production-possibility' of rice will depend on these. The smooth progress of the current Multi-purpose scheme at Gal-Oya, unhampered by archaic land systems, deficient skills or inadequate capital equipment, is a pointer that reliance on these sectors is not foolish. On the credit side, the major internal gains are bound to appear more after the 'initial barriers' have been passed. The great gain on the balance of payments side will be the fact that the type of the new internal production will cut out most of the existing volumes of imports. The present exports will be then largely utilised against import of capital equipment and



certain special skills. With proper co-ordination of development the chances of success are there. We shall discuss this in later pages too.

The problem of full employment emerges as a many-sided one from the foregoing chapters. The present structural background is seen to be unequal to the full-employment tasks. In what follows, we shall attempt to work out an industrial and employment policy appropriate to the conditions. In the interests of having a clear-cut and coherent outline, the method of treatment will be with reference, chiefly, to Ceylon. In course of presentation however, both by way of comparison and otherwise, parallel references to India will be made implicitly or explicitly. This, we expect, will give a broad idea of desirable policy there too.



## CHAPTER TEN

# Policy for Full Employment

## THE STRUCTURAL FRAMEWORK

### Rectifying the Impediments

**T**HE ideas we attempt to set down in this chapter arise from the analysis of the preceding ones. The impediment to full employment was seen to be in the lack of diversification and of integration in the economy. By lack of diversification was meant primarily the absence of wage-goods industries. By lack of integration, we referred partly to the relative fewness of the 'stages' of production ; but mainly to the serious absence of those things necessary for both increase in output of existing units and emergence of new units of production. Prominent among the background features were the rigidities in land organisation, in agricultural production, its marketing and sale, in the over-all financial mechanism and in the economic organisation. The natural consequences were under-employment and low standards of living.

### Population

Before we outline a 'framework', we may set down certain 'Key-note' points that should form the basis of development policy. First, we refer to population. The rigidities in agriculture were due to the predominant dependence of the population on this sector. They were greatly intensified by the steady increase of population. This has been a matter of considerable uneasiness among agricultural countries. Its implications were mentioned in Chapter 6. The conspicuous strides in public health and so on reduced mortality rates. There was, however, no reduction in birth rates. The Social organisation, customs and mores—markedly inclined, except for the taboo on widows re-marrying, to maintain high fertility—did not change concurrently. Industries and towns did not develop conspicuously. On the contrary, the displacement of several handicraft industries helped to lower standards of living even further. In short, the conditions for low mortality were introduced, but those for low fertility were left unattended.



Experience substantiates an inverse correlation between standard of living and fertility.<sup>1</sup> The decline in fertility is generally accepted to follow that in mortality only after an interval, but 'consequent upon industrialisation the rate of population increase slows down.'<sup>2</sup> In the West, the transition from high mortality and high fertility to low mortality and low fertility took about 300 years. In Japan the corresponding period is estimated to be 'less than a century and a half.'<sup>3</sup> Yet, the population 'may double before the rate of increase slows to that of the more developed countries'.<sup>4</sup> The present rate of increase in population should not, however, be any reason against industrialisation. In the end, the threat of 'explosive' population pressure can only be met by industrialisation.

This is not an argument for complacency on the population problem. Firm measures, direct or indirect, to control population growth immediately may be necessary. For instance, on the same basis as Japan, China is expected to have one billion population in 2000 A.D.<sup>5</sup> Our purpose is only to emphasise that nothing in the data deprecate us discountenances industrialisation.

### Savings

The relationship between incomes and value of investment is a firmly established generalisation.<sup>6</sup> In India and Ceylon, the low level of incomes did not permit substantial accretions of money capital. The higher the incomes, the greater the capital creations possible. On the other hand, the high capital creation is required to produce high incomes, especially as the extent of foreign borrowing is limited by several considerations. In this connection, an important point on the possible volume of savings must be mentioned. The volume of savings in these countries is not determined simply by the difference between Income and Consumption in

1. c.f. F. W. Notestein. "Problems of Policy in relation to Areas of Heavy Population Pressure" in 'Demographic Studies of Selected Areas of Rapid Growth' (1944) page 147. Also c.f. Colombo Plan, page 9.

2. c.f. F. Notestein & Others. "The Future Population of Europe & the Soviet Union", League of Nations (1944) page 26. And, H. Butler "Problems of Industrialisation in the East with special reference to India, French India, Ceylon, Malaya and the Netherlands East Indies". I. L. O. (1938), page 70.

3. Journal of Farm Economics 1949 page 247, "World Population Trends" by C & I. B. Jaenber.

4. H. G. Aubrey loc. cit, American Economic Review, May 1951, page 270.

5. Ibid.

6. c.f. Colin Clark, Conditions of Economic Progress, page 12-13 and Chapter 11.



money terms. The under-employment in agriculture represents, to the fullest extent, the level of 'savings' possible in human resources.<sup>1</sup> The re-organisation of land holdings constitutes a capital gain for which no equivalent in money savings may be found except from new money. Given a modicum of technical adaptation on the farm, output would increase. These processes provide resources in investment without touching the relationship of existing income and consumption. Thereafter, it is a matter of economic and financial policy. The only point about these 'hidden savings' is that they are less fluid or mobile than the normal money savings. That they must be reckoned in estimating capital available, cannot however be doubted.

### **Demand for Income**

One of the features assumed in development must be a reasonably elastic demand for income in terms of effort. It has been noted previously that when incomes on small-holdings rise, outside labour may be called in and the income of the small-holder himself remains about the same. When increased income is dependent strictly on increased work, this tendency is probably natural to labour in all countries. The tie-up of increased efficiency to increased wages is a problem in trade union bargaining and attitudes too. The path to full employment is likely to be strewn with such hindrances. It would be wrong however to accept that as one of the 'invariables.' There is no economic law making 'naturally' for full employment. Much of the economic development in the agricultural country is to be consciously created. A change in the elasticity of demand for income is, within all possible limits, one of the things to be effected. There seems no reason why with all round development, that is with more nourishment, more conveniences and amenities in work, off-setting of climatic and other strain in the course of work and so on, the change should not take place, wherever the rigidity exists. Besides, with economic development the same amount of human effort in terms of calories is likely to secure a higher income. A day's work with a tractor or a harvester is an example. The monetary cost of these should not, of course, compare unfavourably with that of outside labour. That will depend on all-round economic development and transfer of redundant labour to more productive occupations.

---

1. Cf. Dobb, 'Soviet Economic Development'.



## Industry and Agriculture

Development must be both in industry and agriculture.<sup>1</sup> The task of agriculture would be to increase its productive capacity, through improved techniques and release of labour for the other sectors. In addition, it would provide a large part of the demand for the new output in all sectors. The task of industry would be to use the surplus labour and to provide a similar high demand for new output. These alone do not create the new standard of living. The tertiary sector is very important too. So much so that a strong correlation has been claimed between high standard of living and a high proportion of the working population in that sector.<sup>2</sup> While that is accepted, it is necessary to limit, in one important way, its implications for India and Ceylon. The above generalisation should not be interpreted to make a statement on cause and effect. It is the high level of demand that creates a large tertiary sector, and not the other way round. The trend, historically, has been first an increase of incomes in the primary and secondary sectors. The increase in the tertiary has been via the secondary sector. Industry will not account in the end for the whole of a given standard of living; and the tertiary sector may be a sound index to a country's economic position. It would seem, however, that industry is the pivotal sector. It is industry's co-ordination with agriculture that can produce the initial appropriate re-adjustment of resources and level of demand. The tertiary sector coming in strength before the secondary is putting the cart before the horse. This point is emphasised because development policy based on agriculture and 'services' comes dangerously close to the type of full employment policy based on the Keynesian 'devices' referred to in an earlier chapter. They were found to be unacceptable.

## Planning

We argued out a firm case for Planning in economic development. The significant point was the need for co-ordination in the investment. Reference was also made to the severe limitation of

---

1. c.f. Lewis loc. cit. page 124. "An agricultural and industrial revolution always go together, the first releasing the labour which the second draws of the land."

2. Colin Clark, op. cit. page 7 and Chapter 5.



capital, emphasised by the steady increase in population. In such a context, the pace of development becomes very important. So also does the need for co-ordination. It is not enough for the State merely to know the desired policies in the various lines of production, finance and so on, and to implement them as and when finance and enterprise permit. The rate of development has to be the fastest practicable to cope with the increase in population and enable higher incomes and more capital creation. In view of potential inflationary or balance of payments pressures, the rate itself depends a lot on the correct allocation of resources as well as on the maximum investment of resources.<sup>1</sup> Action in all lines of investment must be worked out at the same time and carried out in relation, one to another. Some lesson of this sort seems to be keenly recognised in the following passage<sup>2</sup> for instance. "An apparently small difference of emphasis in policy might make all the difference to the direction in which the economic system actually moved." "This implied . . . that the question of dating a particular answer was of prior importance . . . the same answer could be wrong at one time and correct at another." Besides, the sense of urgency was also there. "The situation that Soviet economy had reached was regarded as one of those crucial stages in the process of history when (progress) has to be made under the impetus of an initial rush ; where the inertia-forces (of a whole) preceding epoch of history have to be overborne by the momentum of this sudden movement, if they are not to retard and deflect the course . . . over several decades." Co-ordination needs to be not only in terms of items but also of time.

### Output—Agriculture vis-a-vis Industry

Another important point may be mentioned. The process of development must studiously avoid marked shortage in output of agriculture or surplus in relation to demand in the other sectors.

1. "The quickest way to ease the strain on the foreign exchanges, and to reduce the dependence on foreign borrowing, is to plan the new investment in such a way that its produce becomes rapidly available and add to exports or can be substituted for imports." Lewis, *ibid*, page 126.

c.f. again Dobb, Page 234-5, who points to measurement of Investment not only in terms of quantity but also the "length of time over which the labour and resources initially invested have to be stored up before they eventuate in an addition to final output."

2. Dobb. "Soviet Economic Development". Pages 206 and 244.



The responsibility will be both with agriculture and the other sectors. This idea of 'balance' between agriculture and industry is, probably, one of the most notable concepts recently brought into relief—a concept drawn by Dobb, for instance, from Russian experience. The earlier shortage of agricultural produce and the more famous reversed process, later, of excess food in relation to manufactures, known as the "scissors" crisis, brought the implication out very clearly. Earlier, peasants' incomes were less, on account of agricultural shortage; urban demand too, for manufactures, was less because of the increased money spent on food. Later, under the "scissors", there was a fall of agricultural prices and consequent narrowing of the village market. Remedies involved measures to cut and keep down industrial prices and what was termed goods intervention (that is, imports of goods from abroad).

### Size

During the period of shortage, there was the problem of inadequate grain purchases — born of the very disappearance of the large estates and the decline of the Kulak, and the increased consumption in the more egalitarian villages. The solution was the State farms (later largely given up) and the collectives. In the immediate context, however, the State farms (huge giants of 140,000 acres sometimes) made a great contribution, through the marketable surplus, to economic development. The abolition of Zamindari in India makes this Russian experiment<sup>1</sup> of deep interest from the economic point of view. The type of farm or plantation unit is likely to influence the export capacity and therefore the balance of payments. This would follow from the principle that a departure either way from the optimum size is to be avoided. In this connection, therefore, we shall be referring to size in the 'plantation' industry. We shall, also, briefly discuss the size of the units to be broadly chosen in implementing the industrialisation process.

### Risk

We have also seen the extravagant rates of interest, especially in rural economic life, as well as the special risks of investment. The history of the Managing Agency system, for all its impressive

---

1. Dobb, pages 157, 167, 173, 216 & 224.



successes, is also evidence of the shyness on the part of normal under-writers and financiers on the Stock markets to play their part. In the process, cause and effect became confused. The prevalent financial system became responsible for the high interest rates, the high profits demanded and the risks attached to competition by outsiders. Often, the risks are due to special conditions of soil, terrain, rain and wind, which require adaptation of technical methods to the conditions. But, private investment was made largely on experience of the past. The difference between 'private' and 'social marginal net product' was neither utilised nor conceived. The solution is a co-ordinated programme of development aimed at creating the requisite balanced and integrated structure.

### Isolationism

A final point may be mentioned. It will be noted that at no stage has it been suggested that the economic programme involves reduction of present export categories. On the contrary their essentiality is confirmed. This Thesis is not therefore one of economic isolationism by any means.<sup>1</sup> In fact, our desire throughout is to see a balance of the payments at a higher level and an achievement of the highest practicable export capacity. That should be clearly remembered. Our criticism against the export industries is regarding any claim that they can earn a full employment income for the country.

### Basic Industries

The foregoing features constitute the background into which the structural framework would fit. The first point now is to decide what items of agriculture and industry are basic<sup>2</sup> to such a framework. On the normally accepted concepts, the basic

1. c.f. This endorsed e.g. by Nurkse in *American Economic Review*, May, 1952, page 576 in "Some International Aspects of the Problem of Economic Development." The author concludes "World income is a more basic criterion of world prosperity than the volume of international trade."

2. On the feasibility of determining the lines of demand and size of output c.f. the following by Dobb, Page 5. "The largeness of the unit (measured in its value) in which wants are supplied relatively to consumers' total expenditure (e.g. a motor car, a house, a refrigerator) will have a similar significance in the context to which we are referring." "If motorcars (of a certain type) are to be produced at all, it is desirable to produce them at least in quantities equal to the output capacity of one (large) specialised motor plant. If more are required than this, then the



industries must be iron and coal. The absence of these is assumed to indicate perpetually low economic levels. For an economy geared to the production of industrial goods in exchange for which it expects to get its needs (of food and drink and raw materials) satisfied, the idea is, as far as it goes, consistent and sound. It is the basis on which the national output and, through it, the national income can be made to increase. In the agricultural country, that is far from the truth. Nor, are our export industries a basis for a larger output guaranteeing a larger national income. As already explained, the basic industries here must be the wage-goods industries, the products of most of which come now as imports. In the absence of these, investment activity, especially in domestic industries, can lead to considerably inconvenient results. We may look at the point thus. In an economy, a careful study of all the relevant factors will yield a long list of industries, running upwards, from the lowest-cost venture up to the highest-cost one. Somewhere down the scale, a point will exist, below which Ceylon is competent to produce goods for sale. Now if all these happen to be 'domestic' industries, to invest in them forthwith would spell serious economic difficulties; on the other hand, if all these were either 'export' industries or 'import' industries (the latter we take here to coincide roughly with wage goods) they would warrant immediate investment. The existing export industries lie in this part of the list, but they are inadequate for national economic purposes. Some new industries will probably exist and be very helpful. That their contribution will be adequate to solve the problem is, however, far from certain. The concurrent adoption of suitable 'import replacing' industries is called for. Even if these had not been in this lower part of the list, investment in them may become necessary for the soundness of the economy (we shall deal more with this in the next chapter). In

---

alternative is one of doubling the initial output by constructing a second plant, and then again trebling it; but intermediate levels of output are for practical purposes excluded from consideration."

"The combined set of wants for houses, furniture, gardening equipment, radio, facilities for cooking and eating at home, which constitute one 'mode of life' and another set consisting of flats or lodgings, motor-car, restaurant feeding, public places of entertainment, etc."

Again Page 16, "Decisions about the distribution of a given total of investible resources, in other words, would be primarily concerned with the question as to how many product-types or product-varieties (each in most cases the work of a specialised plant) to put into production rather than with the proportions in which different commodities were to be produced."



other words, given the inability of exports to meet the situation, this institution of wage-goods industries within becomes essential. A broad classification of such industries in this country would be rice, other foodstuffs, fish and clothing—involving the expansion or institution of rice and other cultivation, meat and dairy products, fruit, jams and sweets, beverages etc., sugar planting and refining, fishing, cotton and silk cultivation and manufacture; salt manufacture, furniture, brick, tile, cement, paper etc., certain chemicals and so on. It will be noted that the industrialisation involved will be of an elementary nature, though certainly entailing large resources (including capital). It is also likely that once industries are firmly established, export trade in some of these may develop. Export trade in salt, raw cotton, tinned fruits and nuts, shark oil and so on may exist side by side with new export industries like say, Cinnamon-Tea, Rubber-goods and so forth. But for initial price obstacles, several of the basic industries will not probably be high-cost projects at all and will be able to compete in foreign markets. This essentiality, however, is determined not by this consideration but by the fact of their being basic to the structure. (Where all these are high-cost, it yields in a context of inadequate exports and low standards and rising population, an insoluble situation which has presumably, to be met only by decimation and famine.)

Before we go to the application of this concept to the practical situation in Ceylon, we should consider the difference in respect of India. There, too, the exports are unable to satisfy the requirements, but it is not wage-goods industries alone that are basic for the future economic policy. With vast mineral and power resources and a market potentially greater than that of any country in the world (save China), 'iron' and 'coal' and not merely food and clothing must become basic industries. Even there, investment in the former must, without doubt, have to be only concurrently with investment in the latter. The only exception could be a situation where manufactured exports would buy wage goods. But this assumption as something holding good for immediate policy is incongruous for an agricultural country. So, in Ceylon, while the aim of the basic industries is to replace certain imports, in India it is also to create the foundations for large scale manufacturing industries. The functions performed by the basic industries in the economy are bound to be similar, though more



restricted in the Ceylon context.<sup>1</sup> Increasing purchasing power will in both cases work out their multiplier effects largely within the economy, causing, in India, both industrial and agricultural output, while in Ceylon it will be largely agricultural and elementary industrial goods, most of the other demand for industrial goods here being met by imports. The fact, that unlike India, Ceylon's exports, despite fluctuations, constitute nearly half the national income (with export values per head being far larger than is the case in India) would modify the disadvantage which India would have through absence of large scale industry. On the other hand, this relative ineffectiveness of Indian export vis-a-vis national income, makes it urgent for that country to produce not only agricultural but also industrial wealth.

The meaning of diversification is the institution of basic industries, as here defined, in a way that will render the external effects, of any increase in internal investment for domestic welfare and the internal purchasing power, (whatever the proportions) *well within the capacity of the possible export industries to contain*, and enable the internal effect to register the multiplier effects expected. In this sense, diversification is as sound a programme in a country like Ceylon as it is in a country like the U.S. The scope for domestic 'welfare' activity is also as uninhibited in the one as in the other by any limits other than actual human and material resources.

That the basic industries should be identified with the present imports is not a general proposition but valid only according to the circumstances of the case. There are, in fact, a few prominent items in respect of which most of the resources have to be found inside, e.g. those items in the 'domestic' industrial field which fall within this basic category. Additional road and rail transport, electricity, new housing, are clearly required for the setting up of the

---

1. Theoretically if we pursue the concept of diversification to its logical conclusion, there is no reason to exclude the heavy industries of the 'earliest' stages of production from an economy. The problem is really one of sufficient means to match the ends and partly of global over-supply of capital goods machinery. In a sense, it would be more correct to describe every economy as needing to have all—heavy, light and consumption industries; only some will be specialising in one and some in another. To this extent the simple formula of labour-intensive in agricultural countries and capital intensive in industrial countries will need appropriate adjustment. The vital determinants in the final decisions on the proportions of labour and capital are, however, the objectives of 'standard of living' and full employment—mentioned below in the Chapter on Planning.



basic industries. The mistake would be in considering these items in themselves without the wage-goods industries. As we proceed we shall also see the need for other industries necessitated by the structural set-up proposed. Among them, we mention Fertilisers, Bottle manufacture and small-scale Agricultural equipment (c.f. implements under Japan's method of rice cultivation mentioned later), requirements for replacement in industry and agriculture and so on. Some export industries too (e.g. Ilmenite) may obtain priority with basic industries if they serve the fundamental policy, of being effective tools in achieving full employment (c.f. Chapters 7 & 12).

Ernest research, on raw materials and by-products, can add to the list. It is impossible to anticipate the innumerable objects of investment that should follow in a dynamic economy.

### Economic Re-organisation

Let us now consider the subject of agricultural reorganisation. Its problems centre, on the one hand, round low yields and absence of mixed farming and, on the other, the size and tenure of holdings, lack of capital, surfeit of middlemen and attendant problems. The first step is to decide what would be an optimum holding.<sup>1</sup> This depends partly on technique. In any case, it is clear that the present small sizes of holdings and their fragmentation must be done away with. Up to a point, there is only one way of doing this. It is by consolidation of the strips, and where the area is still too

---

1. A typical instance of the new outlook among "all governments today in India" is the report of the 11-Man Committee appointed by the Government of Cochin in 1947. The complete association of ownership with cultivation; primary multipurpose co-operatives for every adjusted debtor, joint farming both to aid co-operative farming societies and organise collective and State farming for creating joint cultivation especially among uneconomic holdings; an old-age insurance scheme (as in Bulgaria) for every member of a co-operative; and so on—these are the clear underlying trends of thinking. Swatantra, March 12th, 1949, Page 14—16.

In these days when 'revolution' and forcible nationalisation of land are no longer new ideas, even modest governments cannot well blush to strip hereditary rights of some of its 'vestments.' c.f. Lewis *ibid* page 123. All peasant countries with small holdings "have to go through an agrarian revolution at the end of which is some form of large scale agriculture, whether it be the capitalist farm, or the collective farm, or the state farm, or merely the family farm, working large areas with machinery but without hired labour." The writer then refers to some recent 'revolutions' where unfortunately "large estates are broken up into small uneconomic holdings sometimes not exceeding five acres with disastrous effects on productivity".



small, by physical enlargement of the holdings. Such a re-organisation may give an optimum size for a family. There may be certain other economies, however, which even this size may miss. The desirable size for, say, cotton or sugar may be different from that for rice. In areas suitable for tractor farming the optimum is likely to be a larger-scale unit. The advantages of such economies may be reaped either by further consolidation and grouping or by co-operative enterprise. Both have precedents in various countries and both have been successful. Further, in considering what is the ideal holding, something more than present technical efficiency and conditions of cultivation must be presumed. The present high rents and exorbitant rates of interest, the high costs of marketing and sale and the poor capital equipment have to be replaced by more enlightened organisation and assistance. Both State action and Co-operation are urgently needed in the tasks. The measures will include greater association of ownership with property in place of tenancy bases ; it will also include co-operative credit, co-operative marketing, and so on, as well as State guarantees of markets and assistance in sale ; finally, it will include large capital projects in irrigation, clearing, drainage, and other capital assistance programmes by the State.

The following Table,<sup>1</sup> comparing earnings in Ceylon of small holders, tenant farmers and agricultural labourers, may be of some interest.

---

He is pessimistic about the possibility of 'revolutions by consent' resulting in economic allotments. However case reference of such changes by consent exist in the Swiss economy and are worth study.

c.f. Report of the Federal Department of Economics—Agricultural Division prepared from the Cantonal Reports, entitled *Les ameliorations foncieres de la Suisse 1913-1924*; c.f. also *L'entreprise d'ameliorations foncieres de la region de Coppet Nyon, 1943-48*; the reports of the *Societe Vaudoise d'Etude et d'Encouragement des Ameliorations Foncieres, 1945 and 1948*.

1. Sessional Paper 11 of '50 page 49.



Comparison of the Earnings of Small Holders, Tenant  
Farmers and Agricultural Labourers

Small Holder in Colonization Scheme—Family with a Man,  
Woman, and Child (Working Part Time).

5 Acres Paddy, 2 Acres Highland.

Paddy

5 acres Maha	125 bushels	
2 acres Yala	60 „	
	<hr/>	
	185 „	
@ Rs.	8 a bushel	Rs. 1,480
	<hr/>	

Cultivation Expenses

Outside labour for harvesting Maha	Rs.
20 man-days	50
Manure	70
Miscellaneous	30
	Total Rs. 150

Nett Income Rs. 1,330.

Highland

1 acre cultivated with chillies	
would yield	Rs
5 cwt. dry chillies	Rs. 300
Less Outside labour 30 man-days	75
Manure	25
	<hr/>
	100
	<hr/>
	Nett Income Rs. 200
Total Income Rs.	1,800 per annum
or Rs.	150 per mensem.



## Tenant Farmer Cultivating 5 Acres of Paddy Field

5 acres Maha		100 bushels
2 acres Yala		50 "
		<hr/>
		150 "
Less Seed Paddy		18 "
		<hr/>
		132 "
Expenses on account of buffaloes		12 "
		<hr/>
Nett yield		120 " per year
Cultivator's share	120	
	<hr/>	= 60 bushels
	2	i.e. Rs. 480 per year.

Rates of Wages in Government  
Agricultural Works

	Rs.c.	War Allow.	about	Increment Cents	
Men .....	1. 0	...	1.50	...	4
Women .....	0.76	...	1.17	...	4
Child .....	0.68	...	1. 5	...	4

A wage earner employed under Government on agricultural work would receive:—

Rs. 60 for 24 days at Rs. 2.50 p.d. for a man.

Rs. 40 for 24 days at Rs. 1.50 p.d. for a woman.

Rs. 100 for a man and a woman working 24 days.

They are also eligible to receive a 2 weeks casual leave and 2 weeks medical leave with full pay and annual increments of 2 cents.



On the other hand, the Director of Agriculture was able to affirm as "proved" that the average size of the farm should be "10 acres, perhaps 15." The income from 10 acres is estimated at Rs. 500 a year.<sup>1</sup> Sufficient detail is not provided but presumably the figure is for tenant farmers.

In reckoning the optimum size, the contribution of cottage industry should also be considered. Seasonal unemployment is the chief reason for cottage industry. Its role in the economy could be considerable, both by reducing pressure on the land and by controlling the numbers that will have to be taken on to the other sectors. In discussing the foundation of Japan's later development, one writer observes that "those who lived near the sea-coasts combined fishing with agriculture and nearly all the peasant families carried on subsidiary industrial pursuits".<sup>2</sup> Cocoon raising required skill but little capital or material resources. At a time when little additional land was available for cereals, this outlet was most valuable to the Japanese peasants.<sup>3</sup>

Japan has been cited by this author as "a good example of how quickly massive new industries may be built up on the basis of a nucleus of organising capacity and craftsmanship and of a mass of docile, unskilled workers."<sup>4</sup>

Once an optimum size, or sets of optima, are decided on, it would be easy to see what population the re-organised land could hold. It would not be sufficient however to be satisfied with this re-organisation and the attendant increased output therefrom. A far greater output is called for from agriculture. Only part of this problem can be solved by extension of cultivated area. The reason for saying this is as follows. Assuming the present man-land ratio (i.e. total cultivated area divided by population) in Ceylon to be not more than .5 acre the maximum area cultivable will only double this ratio.<sup>5</sup> With an annual increase in population of 200,000, even

---

1. Administration Report, 1941 (Part IV) page D12.

2. G. C. Allen, A Short Economic History of Modern Japan, page 12.

3. Page 110.

4. Page 156—7.

5. c.f. Chapter 9 above.



this cannot long be maintained. It is true that the greater part of the new extensions will be for food alone. Yet when, as planned, 200,000 to 250,000 acres are brought in by 1957 the addition to the population would have been 1,200,000.<sup>1</sup> It is very clear therefore that intensive cultivation is extremely important. A more balanced agriculture than exists at present is desirable. The advantages of the re-organisation mentioned above must be exploited to the fullest. In addition to distribution of high-grade seed and stud for cattle, there must be a large-scale introduction of artificial fertilisers.

Thus, the Fertiliser industry becomes another of our basic industries. The remarkable role of intensive agriculture in the development of an economy was best illustrated in Japan. By 1913 the pattern of imports had changed to predominance of raw materials and semi-manufactured goods and a marked reduction in manufactured goods. But the most surprising feature of the trade was that despite "the large growth in population food and drink imports formed a smaller proportion of the total in the years just before the Great War than they did in the early eighties. This demonstrates the success of Japan in raising her food production from agriculture and fisheries to supply her growing needs."<sup>2</sup>

Another important one among the basic industries is fishing. Here too a great deal of thinking remains to be done in deciding the optimum sizes for units in the industry. The scope for large-scale units is great. There is also the problem of seasonal idleness as in agriculture. With re-organisation and some mechanisation, there is no reason why an export trade should not in time be developed. There are cases of this nature in Japan and even India. Ceylon at present, is a heavy importer not only of rice, but of fish, several pulses and spices, sugar, meat, dairy produce and so on.

It is important that the developing economy must have the basic categories; it is round these that the others must be built.

---

1. Colombo Plan, page 29.

2. G. C. Allen op. cit. page 88. c.f. also page 157. c.f. also the enthusiastic adoption in 1952 by India of the Japanese method of rice cultivation for general application. This may lead to several small-scale industries making items like weeders, threshers, shellers and polishers. c.f. Eastern Economist, February 27, 1953, page 341.



### Location

The agricultural re-organisation, we said involves not only the grouping of uneconomic fractions of land, but also the elimination of surplus population on the land. The two relevant questions arising are the immobility of labour and, inversely, the location of industry. The latter is called for, on the land by the seasonal unemployment. Further, a state of affairs where under any circumstances, land, is inadequate will involve the question of the location of industry (cottage or large). The degree of physical migration of labour will be determined partly by the need for it in other areas, and, probably more, by frictional factors and by general inertia. In the latter event, the need for supplementing agriculture by rural industry becomes more emphasized. In the plantation industries, the device adopted was that of indentured labour from India.<sup>1</sup> It is possible that if the local population were given small allotments to grow these products, the recourse to indentured labour to solve the problem of mobility may not have been necessary. The success of the sugar plantation schemes in Fiji (mentioned elsewhere in this book) encourages this impression. To generalise, all zones with heavy population, or hilly regions which, even if thinly populated, cannot benefit by any devices of mechanical cultivation, must, if they are to be 'rationalised' depend on the twin foundations of intensive agriculture and cottage industries. What these industries are, must be decided in the larger context of the economy. One range of products would be goods substituting imports, like clothing, silks, etc.; the other, export goods—like arts and crafts, and so forth. Both are good and desirable. At no stage, however, can provision of rural industry at the door step, (the inverted mobility of labour) be at the expense of the harnessing of the requisite labour for the larger projects, industrial and agricultural necessary to the background of the economy. The assignment of fields to cottage industries must not clash with those

---

1. The debt of the economy to this labour is seen from a fresh angle by the following discussion of Britain's balance of payments difficulties after the war. In 1938, more than a quarter of Britain's exports were coal and cottons and woollens. If there were the same volume today, there would have been no adverse balance. This could have been achieved simply by allowing about 200,000 workers into the country, on condition they went to work on essential industries. If this 1% of the working population had gone in, the country would have been free of rationing and other consumption controls, and would have also greatly contributed to European recovery. (Lewis, Principles of Economic Planning, page 84).



to industry. One observation, by W. A. Lewis, on the subject of mobility<sup>1</sup> is worth noting. He finds no evidence for the suggestion by "many people" that full employment makes labour less willing to move. He asserts, on the contrary, that full employment is more usually associated with an excessive turnover of labour; and that it is the universal shortage of houses that is at present holding down mobility. However, this relation between mobility and full employment is not considered valid during the period of the "big readjustments, demanded by the war and reconversion." In Ceylon, therefore, the problem of securing mobility remains one that must be tackled by positive measures.

In the transfer of population from agriculture the obverse side is the secondary sector. The problem of the secondary sector is essentially one of creation of it. In this the problems of mobility and location play an important part. Location and the economies of production are inter-related. A comprehensive appraisal of what should guide location of industry, will involve consideration at more than one level. Basically, there is the well known index that units (farms or factories) must be at the places where essential factors for their activity are present. Crops must have appropriate geographical and climatic conditions for location to be decided. Industries must have most of the heavy cost elements constituting them at hand or within easy reach. Coal and iron being the heaviest items in large scale industrialisation, location has so far been decided by these rather than by the presence of raw materials or labour. With hydro-electric power, the earlier considerations lose much force, and more so if the raw material is also away from the site. To that extent, the possibility of industrialisation for several agricultural countries becomes more attractive. In Ceylon, for various reasons, already mentioned, the industrialisation contemplated is of a light order. For zones beyond the reach of the forthcoming hydro-electric scheme and power from multi-purpose projects, the prime considerations determining location need not be iron or power, but rather the existence of the raw material and of labour power<sup>2</sup>. Fundamentally then, agricultural projects

---

1. Page 85, *Ibid.*

2. Interesting lessons from Russian experience are discussed by Dobb, not necessarily paralleled to our case but showing nevertheless that rule of thumb methods are not always correct.



will be started where the appropriate soil and allied condition exist best, and the factories where the relevant raw materials lie. It is not often realised that land transport of raw materials, even in small countries like Ceylon is costly. It implies that even in areas under hydro-electric power, the raw materials must exist in their zones and they should not claim to replace other areas as the appropriate industrial sites for any and every industry. Cement is a case in point.

All this is stating the matter broadly. There are other considerations which must strongly determine final location. They may be classified at the following levels, namely, Industrial, Town and Country Planning and the National. The fact of external economies (external to a factory and to the industry) arising from the siting together of several units is well known. It gives a strong case for concentration of industries. The point is valid, but it can easily be carried too far if other considerations stand against such a policy. We have referred to one or two such considerations above. Pushing the argument of concentration for external economies to its extreme, it may be deemed necessary to have all industries in one spot in the country and no where else. On the side of arguments for dispersal, the evil effects of industrial concentration on city life, and of the corollary effects on the health, psychology, efficiency and productivity of the population are today no longer controversial matters. The juxtaposition of work and home (and places of leisure and recreation) and not of factory and factory is the objective. In that sense, there is every reason for location to be dispersed over various towns than over one large sprawl. This would not conclusively prove the necessity for dispersal throughout the entire country. But, to repeat what we have noted before, location is in some important ways related to the location of the population itself. Besides, apart from the cogent argument of town and country planning against concentrating most of the population over a period of years into one region, there is also the question whether it is really possible to do so, just on the footing of a conceived policy of concentration and without any inherent urge or reason for the population itself to seek such a move.

Distribution of the population over the country will still exist and, with increasing population, concentration of economic activity in



one zone alone will still leave large pockets of unemployed elsewhere. These pockets present and potential, can be filled only by a suitable policy of location (consistent of course with the availability of raw materials or parallel considerations). There is also the case, referred to before, of location (of cottage industries, and so on) having to be decided by the location of the particular population suffering from the shortcoming of their agricultural activity. If the controversy then is between dispersal as such and concentration as such, it may confidently be said that the Full Employment Policy depends on the former. As for external economies, it may be noted that the juxtaposition of farm and factory which is likely to arise is itself a source of substantial economies, and it is not certain that concentration of industrial units alone would secure reductions in costs very much more than the former will. We must interpose though, that the foregoing in no way constitutes a denial of the absolute advantage, in a particular zone, (for example the area served by hydro-electric power) of industrial units being situated in a manner that would ensure a cheap and convenient tapping of power resources; so also in regard to siting along railway lines or a river. But in securing in the best sense the external Marshallian economies, the other imperative considerations for dispersal must not for a moment be overlooked or forgotten. It is our opinion that most Marshallian economies can be secured at the same time as the economies of dispersal are being secured. Concurrently also certain larger considerations relating to the economy as a whole need to be kept in mind. The siting of Units, especially of farms, has its effect, for good or for ill, on forest reserves and soil erosion. Apart from an efficient system of agriculture, good location is bound to help. Probably forest belts between, instead of stretches of farm land (like the Dust Bowl in the U. S. A.) are required. It need hardly be said that a policy of reafforestation (conducted according to where agriculture is not likely to enter) is an essential requisite for both geographical and economic reasons.

### **The Unit for Industry and Cottage Industries**

An interesting and vital question is whether industry need necessarily be of the large-scale concentrated type as found in the West; whether in several cases it could not be on a decentralised basis. For example, manufacture of silk or "mammothies", tinned



fruit or butter in Ceylon may more profitably be organised on this 'cottage' industry basis. On the other hand tractor manufacture cannot be so organised. There is also a strong case for this 'workshop' basis in respect of large items of textiles and of any specialised manufacture (like watchmaking in Switzerland) which these countries may undertake. Of course, modern methods, tools and power must exist. The 'workshops' could make either suitable finished products, or supply certain parts to a central factory, or use the latter's by-products. Final assembly wherever required is probably always at factory level. The argument is based largely on the economics of labour-intensive methods in agricultural countries and the general indication in favour of 'light' industry. The more natural manifestations of it would be rather at workshop than at factory levels. It is emphasised, however, that all we can make here is a *prima facie* case. As mentioned earlier, and as we shall see later too, in discussing Planning, the requirements of the national income cannot be sacrificed to that of 'employment for all'; 'labour-intensive' ideas could be pursued only in conformity with the principles of optimal grouping of factors in the unit. So that where costs at 'workshop' level are higher than those at 'factory', and unless some reasons like the immobility of labour and consequent pockets of unemployment in particular areas arise, the pattern of development must be on the integrated large-scale model. 'It is', as has been well expressed,<sup>1</sup> 'the capital,labour ratio of the development process as a whole which has to take account of the relative scarcity of the various factors....and not the choice of productive techniques in each productive Unit.' In the final planning and development work a decision on this would seem very necessary.

It is not possible therefore to state clearly what proportion of economic development should be contributed by 'cottage industries'. But it is certain in the face of existing resource patterns, that the degree of use of cottage industrial methods will depend equally on the decisions regarding Size of Units in industry, as on inherent or traditional factors affecting handicrafts and the like.

---

1. J. H. Adler, *American Economic Review*, May, 1952, page 589 'Fiscal and Monetary Implications of Development Programmes' c.f. *American Economic Review*, May 1951, pages 241-2, Yale Brozen—*Invention, Innovation and Imitation*, for an analysis of how both backward and advanced techniques can be 'best practised' in the same milieu of resource and market patterns.



On behalf of small scale industry, we may also add that by its 'dispersion' it helps solve certain problems of location and mobility. Dispersion, 'disperses' certain 'service' industries too. Transport workers, for instance, will be more evenly distributed; and, therefore, also their needs like housing. It enables labour's immobility to be less of a bottle-neck than may be otherwise.

### **Transport and Marketing**

Location is further dependent for its success on a scientific policy of transport and marketing. It is absolutely essential that a Transport board and a Marketing board should sit conjointly with the Resources board and allied staff. Only this will ensure one of the fundamental requisites of a quick as well as a lasting production programme, namely actual consumption of the goods produced. This involves the question of prices, costs, and fiscal policy and not merely production, transport and marketing. Here we mention the latter exclusively as we were discussing location; we shall come to the others soon. A full employment policy does include in its investment programme additional transport and marketing facilities—roads, railways, water ways, collecting agencies, warehouses, storage units and so on. But it would be completely false, as said before to launch on such investment with the aim of using it to 'provide employment'. Careful planning-out of minimum necessities, avoidance of diffusion and waste of capital and labour through haphazard and ad hoc development are essential; so also are the siting of transport in relation to resources to be tapped, of agricultural and industrial units in relation to the line of transport envisaged and the co-ordination of the various types of transport and of the several storage and dispersal facilities.

### **Training**

Another problem in development is training of labour. The difficulties of acquiring skill, have often been exaggerated. "Big industries permit mechanisation and need comparatively few trained men who could if necessary, be got from abroad. Most of the operations of a modern factory can be learnt in a few weeks by the least skilled. The Government itself (India) worked out a scheme for training 48,000 industrial workers at 310 centres by



March, 1943. The Bevin Scheme by which Indian workers are sent to England for an intensive course of training in British factories has been successful, and these Bevin boys are engaged in training other workers."<sup>1</sup> In many jobs a man may now learn as much in a well organised training centre in six weeks or three months or six months, as he learnt in 'olden days' in four years of haphazard apprenticeships. This is now recognised in the establishment of many Government training centres.<sup>2</sup> The quickest and most effective method, for training labour as well as engineers, seems to be to import technical skill. This could be supported by training abroad in selected cases, by more technical education in schools, and by special schools and colleges for advanced technical learning. It is said that in 1872 there were at least 200 foreign technical experts in Government employ in Japan.<sup>3</sup>

The fact remains, however, that over and above the intensive training of a small percentage of the population, the mass of the labour force needs some instruction and introduction into new methods. Often it may be a matter more of uprooting the man out of his conservatism. In this case, social and legal expedients are more necessary—in agriculture, for example, some threat that non-adoption of particular methods in an area would result in the forfeiture of right to the land and handing over to another cultivator. Talking in general terms, we must realize that mobility of labour becomes sensible only if accompanied by training. Even as the policy of location was seen to be necessary to tackle effectively the problem of unemployment, so also, without a programme of training, pockets of unemployment will continue to exist. But facile policies of 'training' alone are utterly insufficient. In fact, training cannot really exist without the factory (or new-type farming) existing and there is no excuse for investment activity to wait till training is over. Nor should excessive funds be poured into training as such, in the name of full employment objectives.<sup>4</sup> It would be much wiser to divert most of such funds into actual erection of the investment unit

1. Lokanathan, *ibid* Page 13.

2. Lewis Principles of Economic Planning, page 81.

3. Allen *Ibid*, page 28.

4. "If...the nation required some 24,000 persons every year with commercial and technical training, it would not be difficult to give such training if every person who left school had at least 10 years' elementary education. The first task therefore is to make compulsory education compulsory." Jennings, *Economic Survey of Ceylon*, Page 175.



and allow acquiring of ability to follow under the guidance of a small group of trained pilot staff or force. The offer of technical aid to under-developed countries under point four of President Truman's plan facilitates and simplifies this aspect of full employment policy and there is every reason for the country not to be dependent for its objectives on first having a standard of indigenous technical skill such as must certainly involve delay.<sup>1</sup> Talking of education, one must not commit the grave error of forgetting the enormous change required in agricultural methods and the relation of education to it. The outstanding example of Denmark, especially its agricultural schools and the widespread adherence to book-accounting should probably be our best guide; the work of the co-operative movement in Ceylon could well form the nucleus. Our problem in this field would be that of combining economy of funds with results.

### Finance and Credit

Higher in priority than general technical education, is an appropriate and efficient finance and credit structure. We have already seen the shortcomings of the existing structure, both in regard to scope and nature. There is no proper money market nor system of industrial finance in Ceylon. While these exist in India, they either do not go far enough or are inadequate in the spheres covered, cumbersome in their response to demands and often disadvantageous to development in the long run. The question of rural credit has certainly to be solved by re-formulation at a more comprehensive level. For one thing, the credit machinery appropriate to small agriculture is not often so to large scale cultivation like cotton or sugarcane;<sup>2</sup> for another, the function of credit must needs be coupled to that of harnessing savings. The need for organising savings arises equally from the needs of industrial credit and the present restrictions in credit facilities.

The establishment of a Central Bank in Ceylon is certainly a step in the right direction. But much of its meaning can emerge only with a proper appraisal of its duties in the context of the

---

1. c.f. the fact that mastering of technique was the object of the Second, not the First Plan in Russia.

2. In regard to the latter e.g. the question of having differential interest rates for storage etc. by preparing schedules of interest rates, has been raised.



economy for which it is meant. Discussion on such subjects often becomes over-complicated, diffused and even irrelevant. For our purpose, it will be sufficient if we make the following observations. The contribution of a Reserve Banking Institution in a country, briefly revolves round three sets of functions: the currency function, the exchange function and the credit function. Everyone of these three functions can in fact be performed in an unco-ordinated set up by three separate bodies, for example, a board for currency, a department for exchange and the banks for credit. The pre-Central Bank (1949) exchange standard created a heavy dependence on the balance of payments for currency stability. It carried with it also the very irrelevance, as Keynes would have it, ideologically, of reserves tied up and never able to be used. It was worsened in this instance by the fact that the reserves are valuable foreign exchange. Internally, there was a lack of proper relation between currency and credit, and exchange resources and credit policy. These things, in the joint result, constituted a serious cause for change. Such change could in effect be had if the currency board, for example, declared a managed currency for the country, compelled by reserve requirements or otherwise response of commercial bank credit to its wishes, and acquired directive power in respect of exchange control. This in fact amounts to creating a Reserve Banking Institution; a consciously created Reserve Bank is just this—controlling policy in regard to currency, foreign exchange and credit. The success of an independently managed currency however, would yet largely depend on the earnings of surplus foreign exchange (and especially of 'attractive' exchange). So that, a balance of payments deficit, leaving foreign exporters with rupee exchange on their hands, is far from attractive to the latter and is bound sooner or later to affect the stability of the currency system itself. Both on the showing of the previous chapters and of what is to follow regarding foreign borrowing needs, judicious control, conservation and utilisation of exchange are very necessary to the development of full employment policy. The biggest argument for a Reserve Bank institution is, however, in respect of the credit functions. What is required is not merely a means of control over the existing banks, but fundamental changes in the depth and breadth of banking functions and services. A special institution of a far higher level



than a currency board per se, able to view the entire economic background, capacity and needs to direct not in respect of a mechanical increasing or decreasing of total credit alone, but to direct on the nature and the lines of the credit flow, to issue sufficient guarantee to cover such risk as may be entailed therein, and if necessary to foster appropriate credit institutions throughout the economy—such an institution is in fact one of the conditions for a rational policy of development and full employment. Subordinated to this controlling and guiding unit, which becomes now the financial First Cause and the lender of last Resort, is the wide ramification to be created if it is not already there. As for the commercial banking institutions, in the modern state of currency and credit regulation, the controversy between unit and branch banks is somewhat out of date. With unit banks having historically developed inevitable interlocking connections of one type or another, the case against branch banking is little. (Attempts like shuttling reduced resources over branches to 'window dress' could be overcome given the assumption of modern credit regulation methods).<sup>1</sup>

The duplication of banks in a given area, however, is a matter to be watched. On the other hand, a far more extensive development of banking is required both for harnessing savings and for providing really useful credit. The War inflation created new sources of national savings in the heart of the rural areas and the most assiduous and careful methods are required to harness them. Mobile banks have been suggested to get at these dribbles from the villages<sup>2</sup> which in the total may amount to a large sum. The idea is worth every consideration as an adjunct to the new branches, over the country, of commercial banks. The mobile banks (to which could also be entrusted National Savings weeks) would, of course be more for collecting savings than for credit purposes.

As a system there is hardly any better than the co-operative credit and sales societies for peasant farming and husbandry.

1. In fact, in post-war Britain, window-dressing is no longer existent—c.f. *Journal of the Institute of Bankers*, April, '47.

2. An interesting new step is the recent proposal in Madras to make it compulsory for land holders to lend to the Government an amount equal to one year's land revenue—returnable at interest in five years. (*Eastern Economist*, December 9th, 1949, Page 387.)



So that, the role of the Reserve Bank in this field would be to provide their banks with re-discount and credit facilities. As for other agriculture like cotton and so on, the Reserve Bank would have to provide liberal facilities through banks as well as specialised Institutions (into which the Land Mortgage Bank, Industrial and Agricultural Credit Corporation, etc., would fall). For ultimate success, this policy would need to be liberal not only in loanable quantity but equally in spirit. Methods like loans against crops yet to be harvested would, if necessary, have to be adapted by commercial banks themselves without hesitation. What is required most is a close and intimate touch with actual activities on the farm and not a mere expertise in application of rules and regulations. Such an attitude is an approximation to the familiar French and German systems of 'industrial' banking, or rather to an extraction of the sound practices thereof. Commercial banks would still be lending against working capital and not fixed capital, though the specialised institutions will accommodate the latter. The point is, however, that for a really enlightened credit policy as called for in the context of a development and full employment programme, close intimacy with the actual use of the loan itself is necessary to provide the requisite confidence to lend. The mere dependence on general credit-worthiness of the constituent is too restrictive.<sup>1</sup> Today, there is a hiatus in the sector of agricultural credit; the existing structure and volume of credit can by no means be said to constitute any useful or relevant reflection of national economic needs.

The problem of credit is equally prominent in the sectors of industry and trade. To the extent that private enterprise plays a positive role, the smooth flow of required credit and not merely the husbanding of savings must take place. For this purpose, the Reserve Bank may need to compel the Credit Institutions to make loans when certain given conditions exist. If so, it also logically follows that in effect the Reserve Bank must be prepared to offer its own guarantee to the banks concerned. It is one more argument for prior planning of the structural set-up contemplated. If the argument is further pursued, a point can actually be reached where the role of the Reserve Bank would well be, in several ways,

---

1. c.f. Russia e.g. "On a large construction site the Industrial Bank will often have its own office and a representative who directly checks all expenditure in connection with the construction work." Dobb, Page 358.



one of instituting and running of the industries themselves. The Reserve Bank becomes at this point another term for the State, and the dividing line between the private units and the existing State industries and farms becomes less discernible. An administratively better method would be to allow the Industrial Credit Corporation or a National Development Corporation to assume the functions of industrial finance, guarantee and management.

It is not proposed to infer at all from this that private enterprise has no place, but it is clearly necessary to reaffirm the proposition of earlier chapters that State participation in and implementation of the development programme is required in a high degree. Any proposed public Corporation should, preferably, include private capital.

It may well be that non-use of credit facilities is not due to the impracticability of loan conditions themselves, but to the reluctance of individual enterprise to embark at all, under certain circumstances, on investment schemes. Such a condition, imposed over the general paucity of capital in agricultural countries, can be paralysing and would today actually seem to exist in India and here. In India, the severe budgetary policy soon after Independence was blamed for a start. But even a reversal in that field of policy-making not having made any impression on activity, the existence of more fundamental forces have been recognised. In regard to working capital, the Reserve Bank could with effort meet the requirements. In regard to fixed capital, the problem is more difficult.<sup>1</sup> Overshadowing these, however, is a paradoxical situation of want on the one side and industries producing at half capacity due to insufficient demand on the other.

Nor can the funds of the specialised credit institutions be said to have been at all stretched to their limiting points.<sup>2</sup> The insufficiency of demand for certain products despite the recent enormous

---

1. "There is, perhaps, an example to be followed in the efforts that are now being made largely under Mr. Nelson Rockefeller's leadership, to associate U. S. and Latin American capital on partnership terms." *Economist*, December 4th, 1948, Page 906.

2. As a fundamental reason for such failure we may point to the absence of a 'plan', of a policy framework constituted in terms of capital, equipment, controls, prices etc. The problem is not merely one of disbursing purchasing power, but of *directing* investment and instituting it.



inflation is probably due to the self-same inflation whose benefit of additional money income is mostly absorbed by the high prices of essential commodities. In certain cases, the holding off of purchases till prices come down later, may be a reason. To that extent this contributes to the fund of savings lying idle and yet to be harnessed. Savings are also created by industrial and commercial institutions in the course of their activity.<sup>1</sup>

It may be noted, however, that though idle savings exist they can by no means be considered a surfeit in relation to the needs of the economy. Idle balances in the Banks only indicate that the unavailability of savings is not the only or the main problem. It is a sad commentary that those balances themselves cannot be used. The shyness of capital, then seems to be influenced by the insufficient demand for goods mentioned above. To pump money in at this stage and create purchasing power for such demands to be actualised will largely result in more inflation ; while some additional purchases may be made, the old insufficiency of demand will generally emerge again. Further, in all high-price situations there is the concurrent feature, on the production side, of high cost of materials and so of production, which certainly would discourage capital risks even if entrepreneurs are prepared to launch out or established industries are prepared to expand. All this combines the features of both a vicious circle and a dilemma. The latter, however, must be eliminated if the former is to be broken. High prices could be eliminated only by increased ratios of output to money. Vigorous harnessing of savings and the concerted increase in supply of wage goods will reduce price sufficiently for the existing volume of money (plus new wages) to absorb output at the new price relationships. Increases in supply after that stage may have to be accompanied by an increase of purchasing power, but the increased supply now cannot afford an unplanned dumping of

---

1. c.f. American Economic Review, May, 1948, Pages 332, 339. H. Jones, "It is necessary to mention the close relation of (reserve policy of the Central Bank) to the adequacy of investment by intermediary institutions. Inadequate reserve policy has contributed to the inadequate investments of the institutions in the past and may do so again." "To keep deviations from optimum investment reasonably low the intermediary institutions should be assured that they can receive from the Central Bank any funds they may need to meet withdrawals at times when investment tends to be inadequate. They must have adequate access to central bank credit to permit them to make all the investment which they are willing to make so long as investment tends to be below the optimum and inflation does not result." These remarks, it may be noted, were made with reference to the far more favourable position of the U. S.



mass purchasing power. It presents a most trying situation, with the necessity to launch out in production now, probably at a high cost, and with the prospect of new production lowering the selling prices. In the long run, the effects of the larger turnover and also lower costs of material etc. in subsequent production activity will encourage production. But to break the ice and throw capital in now is a most difficult problem.<sup>1</sup> It is at this point that not only all the adeptness of a Reserve Bank, but State guarantees of market prices and similar assistance will become crucial.

We may mildly remind ourselves that today we are at this crucial point. It is only one more step to see yet again that the point about State participation and assistance emerges from this angle too. It may be mentioned that one useful device to bring down costs will be what was referred to in an earlier chapter as 'goods intervention'. A smoother and easier start to development could be made by introducing an appropriate volume of imported wage-goods in the Plan. As an influence in keeping price and cost relationships at the desired level it would be a powerful lever. Its limits will be defined by the total borrowing capacity and the amount of foreign capital equipment required. Its usefulness will be entirely determined by the degree to which it is integrated into a productive scheme of concurrent investment and not sought for the limited purpose of curbing inflation.

---

1. The heart of the problem of trade depression and cycle is the discrepancy between cost of production and sale price—a condition where the latter is higher than the former contains rising price conditions, and vice versa. The cause for depression may be termed the sudden stop to higher sale price conditions—through under-consumption. Investment being a prior commitment the advantage of price fall comes first to goods for sale (consumption). At some stage a period begins when with cost of production at the given level, the efficient out-turn of supply relieves shortage (alternatively, produces under-consumption conditions) and prices relax and the economy is faced with the riddle of producing at a 'higher' cost and selling at low cost. The latter is certainly very welcome, but the problem is to make the former also 'low'. The solution works itself out really as enabling production to be bought out at its 'higher' cost—by subsidies at factor level till factor prices themselves go down, as they will, in line with the fall in sale price or cost of living indices.

Alternatively, a crisis may arise e.g. when production is saturated in one line of capital goods; stoppage or rationalisation creates unemployment which hits total demand for consumption goods, which hits all other lines of production. A remedy is maintenance of purchasing power and confining of the derangement to the original line alone. For a progressive policy, however, planning is definitely called for.



### The Plantation Industries

We have so far neglected those major sections of economic activity which have been the key to present wealth in Ceylon. The omission of the plantation industries, tea, rubber and coconut, up to now was, however, with reason. Unlike most of the other sectors of the economy in the desired structural set-up, they form a section that is already in existence and in a form which, generally speaking, is appropriate for achievement of optimum results. Greater use of rubber and coconut in new internal industries is, of course a separate point.

The rubber industry was in 1949 going through a crisis. The very low prices gave significance to the question whether small holdings and not the plantation system was the answer. The resistance of the small-holder in Malaya and the NEI to low prices has been mentioned. The organisational, processing and other economies of large scale production have been pointed out in favour of the large units. One of the chief handicaps in Ceylon has been the comparatively low yield from the trees. There is a need to increase the yield and to replant. The former may be achieved by maximising yield per acre or per tree or both. Attitude and facilities will determine whether the small-holder or the planter will replant more readily and easily.<sup>1</sup> The satisfaction of the small-holder with low incomes should be no argument for one to pass the burden of meeting the depression to that class. Large portions of the industry in 1949 were still well above the 'marginal' level, and the comparison for efficiency must be between these and the successful small-holders.

It is instructive to refer to the case of sugar planting in Fiji. In 1913 an experiment was begun to convert the estate system into one of small-holdings. The idea was to create a contented peasantry with a direct interest in the land. "These experiments

1. c.f. Economic Journal, September 1946, Pages 391, 400, Bauer—"Measured by long period supply price the small-holders are the more efficient class, though their methods necessarily differ from those of the estates. e.g. the much greater planting density on small-holdings reflects the absence of cash wage costs; speaking broadly, the small-holder tries to maximise the yield per acre and the estate the yield per tree..." "Very large quantities of native rubber would be unaffected by a rise in money wages in the Far East, while the long-period supply price may be reduced if high-yielding planting material were distributed to small-holders." These are important considerations in gauging the competitive strength of natural and synthetic rubber.



had such success that in recent times the (Colonial Sugar Refining) company has relied almost entirely for its supplies of cane on the efforts of small farmers . . .” The results are said to be comparable with the high yields in Mauritius and the West Indies. The tenant is under agreement to grow sugar cane and green manures. But a rotation crop of rice is allowed and small gardens round the house are encouraged. Supervising staff exist to assist and to transport the cane to the factories ; houses, advances, manures at cost price, implements at low rates of hire, breeding mules and cattle are all provided by the Company. Peasants help to cut one another’s crops and the charge is debited to the respective growers.<sup>1</sup>

A parallel scheme is that for the Gezira in the Anglo-Egyptian Sudan, also started in 1913. It is a tripartite irrigation scheme for cotton, with the peasants, the Sudan Plantations Syndicate, and the Government as the three parties. The conditions of tenancy lay down that the peasant must use a prescribed part of his holding for subsistence crops, but no charge is made for the use of canal water in this cultivation. There is closer supervision by the Government than on the Indian canal colonies, but this is considered natural in the case of large irrigation works producing for export. The tenants are, however, markedly better off than their neighbours.<sup>2</sup> In this connection, it may be of renewed interest if we turn back to our figures of Earnings of small-holders, Tenant Farmers and Agricultural Labourers, at pages 163 and 164.

Generally speaking, it is possible that tea is essentially a large scale industry. This is strengthened by a recognition that the tea industry in Ceylon had become in the Thirties ‘one of the most progressive, most scientific, and best organised industries in the world.’<sup>3</sup> In rubber and coconut, there may be two points in the ‘curve’ indicating optimal positions—one for a small unit and one for a large. If so, the present structure in these industries which mingles both small and large units warrants non-interference. The emphasis in future activity will then be on planting of high grade rubber, efficient processing, transport and marketing, in addition to increasing industrialisation based on these raw materials.

- 
1. c.f. ‘Colonial Agricultural Production’ by Sir Alan Pim, pages 78-9.
  2. Op cit pages 122-23.
  3. Op cit page 62, quoting L. A. Mills ‘Ceylon under British Rule’.



The inability of these agricultural industries to solve the problem of the standard of living and full employment, we have seen already. That under any set-up, however, their contribution to the sum total of the national income will, to say the least, be large must not be forgotten. It is but wise, therefore, and necessary that this section of the economy continues to contribute its maximum benefit to the economy. To the extent that external factors help or hinder the prosperity of these, the State must needs give all assistance. Before, for example, a sound policy for rubber—the nature and extent of its future production, the new capital expenditure warranted etc.—can be finally set on foot, a definite appraisal of the long term prospects of rubber must be made by suitable technical and planning Bodies. The demand in present consumer countries and among future consumers, new sources of demand like increased transport and manufacture in hitherto undeveloped regions, new uses like rubber for roads, are some of the factors that will control the prospective trend of prices. The usefulness of these industries is also necessarily bound up with the scope and “freeness” of world trade. Certain restrictions or disabilities in trade could well vitiate such policies for them as are based on potential markets. Today, these products sell almost entirely in the dollar and sterling regions. With unhelpful discarding of rubber to the economic wilderness, there is still the possibility of other markets in the world which need the product. The convertibility of various currencies to a sufficient degree, to make the circuit in trade complete, is necessary. The whole question of markets, prices, output will have to be decided in this background. In fact such a change from established markets to new better markets is really possible only in the absence of a fearful dependence of the economy, on these products. That again is stating in different words the case for diversification. We shall have more to say about requirements in world trade structure etc. later on. For the moment, we shall take certain hypothetical states of demand and supply in respect of these agricultural products and lay down the principles that should govern the activity of these industries.

These products display a dual aspect, each one therein an opposite to the other. On the one hand, as the major props of the economy, these industries remain the best sources for taxation to



the optimum limit; on the other, considering the peculiar vicissitudes in their fortunes in the world market, they present a case for assistance. Very often they have touched sub-marginal levels as the period of Restriction<sup>1</sup> clearly indicates. It is necessary to see to what extent restriction, subsidies and so on are economically sound both from the point of view of these industries and from that of the national policies appropriate to full employment. It may be said forthwith that there is no case for restriction or subsidies to be considered in every instance of crisis in these particular industries. The full case may be stated briefly in the following manner. Our means to final full employment have been seen to be elimination of surpluses (of whatever factor) at every point and effecting optimum combinations. We have seen the fields in which future employment is to be directed. If we may anticipate a point to be demonstrated in the next chapter, certain high cost firms (e.g. a rice farm in that position) would if organised as efficiently as factors would permit represent an optimum combination, granted that the alternative is employing factors on digging holes in the ground or on leaf-raking or on any thing less worthwhile to our objective than the rice cultivation.

Now there are certain extremely likely situations when the marginal units in the plantation industries answer to the description of being less worthwhile. If full production according to capacity reduces price to the point of making the industry uneconomic and output has therefore to be contained within a limit, the question immediately arises whether a smaller capacity cannot well produce the required output, releasing the remaining factors for use in the development programme. The land may be used for food and labour for agriculture and industrial manufacture. We may consider that proposition in conjunction with the circumstances under which that will not hold true.<sup>1</sup>

Where the discrepancy between demand and supply is due either to increase in output or decline in consumption, if such discrepancy is *temporary* the urgency and the case for restriction (or a similar mode of assistance) becomes established, (though

---

1. By restriction is not meant reorganising size, etc., of the units to optimal level, which is rationalisation, but regulation of output alone leaving capacity untouched.

1. On all this c.f. Rowe in *Economic Journal*, September, 1930.



the actual nature of the steps is not as simple as is sometimes assumed). For instance, a temporary *surplus* output assumes a shortage soon (the temporary increase is assumed to be temporary). For various reasons, the system of the buffer stock may not work out at all. As we saw in Part I, there is the gap between the merchants' sale price and price paid to produce. Again, there is an abhorrence of the present economic system to the holding of reserve stocks, since merchants are unwilling to wait too long for the expected short crop. They thus 'depress' even future normal crops. When the producers themselves or, better still, the State takes control, the chances are much better. Even here, the short crop must be short by the amount of the previous excess. In practice, cases have occurred, only too often, of reserves accumulating (Brazilian coffee and Malayan tin) the existing prices (which may have an element also of interest on storage of stocks unsold) probably creating new capacity. In the end, this method may lead to permanent excess output. The extreme difficulty of clearing a glut has been called the great drawback of the modern system of specialised production and any attempt to make the consumer pay in the short run has been termed an extremely dangerous undertaking.

The excesses may involve reduction of many more firms, in the long run, to the marginal limit. Rather than a system of stocks, it may be better to go in for a restriction in output itself, or a floor price with the State paying the difference to the producers, depending on whichever, (the price under restriction or the price for normal output minus the State payment to bring it up to floor level), is capable in the particular circumstances of bringing a larger total revenue to the economy. Till the first year of excess, however, deliberate restriction cannot begin. The floor device may thus be found the better method, on the assumption of supplies returning to normal.

Where the discrepancy between demand and supplies is due to temporary decline in demand, the situation may be the result of (a) trends among merchants and middlemen or (b) actual consumption. In the former case, the proper remedy is a centralised marketing organisation or single selling agency to prevent weak selling. So long as its function is limited to minimising loss



by weak selling (and not extended to additional monopolistic profit seeking) the chances of success are always present. The upward revision in 1949 of the U.K.-Ceylon coconut contract under State auspices, for example, really comes under this and is, though in a small way, a forceful illustration of the difference such assistance could make not only to the industry but also to the balance of payments situation.

In the latter case (b) of temporary decline in actual consumption the question is related to supply proper. Holding of stocks suffers risks similar to those seen above. Restriction would appear superior, though in a given case the decision will rest on the cost of stock holding as compared with the increased cost of producing restricted output. In restriction, what was earlier implied again holds good, that only capacity that will shortly be required must be considered valid ; and so new capacity technique etc. must be allowed for before regulating the amount of restriction ; restriction should probably err on the side of too little restriction. Again, the probable superiority of the floor price may prevail ; if the demand decline is temporary, restriction may not have time to operate and the floor system may step in and remain. It may be worth keeping in mind that restriction is to maintain normal price at higher cost of production (since units will be producing at less than optimum level and higher marginal cost) and floor price offers normal price at optimum cost of production (i.e. lower than under restriction).<sup>1</sup> The stocks in the latter case, are disposed of by the lower sale price on the world market. Finally, it may be said that in both the above cases, of temporary discrepancy between supply and demand, the absence of new markets is taken for granted.

We may now take up the case of the discrepancy between supply and demand which is not temporary, but where the phenomenon is one of *permanent* excess capacity. Clearly, the holding of stocks is nonsensical. On the assumption that the full use of capacity will cause a price that renders numbers of units in the industry uneconomic, a case for restriction would seem to exist. But the excess

---

1. The International Wheat Agreement has much to recommend itself for wider application; its success of course depends on the continued mutual self-interest being served of both buyers and sellers.



capacity itself may be caused by improved technique or new and better planting. Restriction, with its *modus operandi* being a discouragement on the latter, gives support to the vested interests of the inefficient units and prevents their disappearance (or their overhaul by reconstructing their capitalisation or subsequent modernisation). It is rightly observed that the final interests of the consumer are not contained in restriction but introduction of low cost capacity (standards of costs being taken from the alternative occupations or uses of resources). It is not incorrect at all, if the point is boldly faced, to see that the final interests of the producing country also rest on the same.

It rests on the principles of utilisation of resources which we referred to in discussing the field for industrialisation and to which we shall further refer in discussing the place of the high cost firm in the economy. Redundant resources, properly defined, have no case for continuation in a unit. In saying this, a full, bold, imaginative and realistic assessment of long term total demand is first presumed.

We also rule out another case where the existing capacity may not be considered surplus. This is the contingency where, in spite of permanent excess capacity, capacity at its optimum output (and of course lower prices) still produces more foreign exchange resources (though less profit to each individual firm) than in the alternative circumstance; namely, where a reduced capacity (and higher price and a diversion of the resources now occupied at the marginal level to other fields) cannot either reduce imports, or increase exports sufficiently to earn the same amount of exchange. In actual fact, however, this assumes that improved technique in production does not take place. The truth may be that a smaller number of efficient units may easily produce that amount which will yield maximum total revenue. Besides, the chances are that diversion of resources to help reduce imports will be more successful. All told, the blind recommendation of support to the marginal units is highly unrealistic. Assistance to more efficient units to speed up efficiency and so raise output to the desired point and reduce prices wherever appropriate, is better policy. Even under a secular trend of rising demand (new markets, new uses etc.) decapitalisation and use of efficient units for expansion of output is logically more sound.



In the case of rubber, for example, it is likely that the existing capacity will turn out to be surplus, in terms of total revenue at selling price. If at any time, all units are running at a loss there is need for support up to the point of maintaining an output consistent with maximum total revenue. In practice, only some will be operating at loss and support may not need to be as wide as in the previous case. It would appear that some firms must fall out ultimately, but it seems also likely that some of the firms required for the future will still be high cost at the moment. Two questions arise (a) Are the sub-marginal firms that should fall out to be allowed to do so, and (b) are the sub-marginal firms required for the future to be supported and, if so, in what way? The essential point about the first is that falling out of firms creates frictional unemployment which in this case may be so large as to make the term 'frictional' little more than technically correct. The falling out of the firms must be made simultaneous with opening up of the new proposed lines of economic development and employment. In other words, the economic aim of rationalisation in rubber is only possible under prior planning of economic development for the country. Till then a falling off of the firms may not be advisable for both economic and social reasons. Restriction would be better, preferably associated with subsidy in the form of floor levels in prices. It may be noted that simultaneous use of restriction and subsidy is sound only in this case or that of waiting for new markets known to arise. In all other circumstances, the correct manner of change is knocking off the marginal firms up to the point required and maintaining full output among the others. Regarding the second question above, where some sub-marginal firms may need to be continued to ensure the required total output, such a case will probably exist only if new markets etc. are known to develop in some future period. The case for subsidies is clear in this case. The position today in rubber may approximate, despite synthetics, to this. If with new industrialisation in the world, new demands in Germany, Japan, Russia and so on, and our own consumption in manufacture, we are in a position to find use for our capacity, the course would be to maintain that capacity now, regulating present output and ensuring reorganisation and modernisation throughout the industry. For this purpose, a



subsidy (say floor price) must be conditional strictly on simultaneous modernisation in every unit (replanting with high grades, effecting economies of processing, marketing and so on).

The State has a large role to play in this as well. Its remissness would be greater the less it is ready with a policy on future output volumes and a Plan of Development for the economy as such.

Enough has been seen in the above to make us realise that attention to the problems of this sector of the economy is both necessary and important. We have, however, not conceived its problems to be the only or the major wants of the backward economy. As a partial contribution (of some importance) the plantations industry will continue to play a vital part. But it must not be mistaken for the wider, deeper and very much more comprehensive, probe into the National Economy that we have throughout adopted, in the midst of which this will fall into its more modest place.

### **Export Industries**

The plantation industries fall within the category of export industries. As we saw in discussing the field for industrialisation, where export industries are possible they are as sound and feasible as import-substituting industries. It is realisation that the economy cannot be rescued by a mere dependence on further exports from the plantation industries that led us to a comprehensive examination of internal economic development on the lines of the earlier pages of the present chapter. In the course of that discussion, we saw that some of these industries could also quite easily develop exports. Fisheries, cotton and the like were good examples; like tea, there was cinnamon tea, which may have considerable scope if accompanied by proper sales machinery.

We also saw that cottage industries (rural industries may be a better term) were from the point of view of optimum combination of factors, of mobility and of location, an important aspect of a sound programme. Some of these like cotton goods and silk, would mostly serve their purposes in the larger economic context as import-substituting industries. But it is likely, that a large range of these will in the long run be actually export industries.



We need not repeat the proper requirements for this, of co-ordination between agriculture and manufacture, proper credit, proper collection, proper storage and marketing. The outstanding question is what type of industries are expected to develop exports. This is one of the fields where constant scientific research is, in modern conditions of world trade, essential. A comparison with enterprise in these spheres in other countries would show the immediate and immense possibilities<sup>1</sup> of export trade in certain items like bananas, cashew nuts, fruits (bottled and otherwise) like mangoes (names with reputation in trade, like Jaffna mangoes, could be put to best advantage, even as Jaffa oranges have been), guavas, mangosteens and a large number of similar items. This would perhaps establish the case for a glass industry in the basic category, being probably more cheap for us than tin, and a case for bottles more than for glasses or other crockery. This involves technical and costing considerations, however, and no ready conclusion can be made here. Of course, the various handicrafts of ola, grass and reed, wood, metal and so on need much stronger support than at present. More patronage (for that is the proper word) must be bestowed by the State, which must be clear in its mind as to what its responsibilities are. For example, it has been estimated that the Vanaspati trade in India, in order to establish its market, spent over three lakhs of rupees in advertising that trade name; today, vegetable oil has more than paid back the seemingly exorbitant waste of funds on the initial popularising of the product. We will need all the sales technique of advanced countries. This studied technique is required equally for tourist traffic which can very well become a most significant source of new export income. Often, we are wrongly led to believe that mere clap-trap and natural attractions are enough. Attractive conveniences of living and moving about, and amenities for comfort and enjoyment are imperative. At the same time, a country in a backward condition cannot spend excessively on building up these conveniences. If for the first few years of tourist activity, we remember that all earnings from tourist trade should go to intensive installation and development of tourist conveniences, we may find ourselves on the correct lines. A quick rise of tourist income may not take place, but the shrewd utilisation now of whatever rises occur will

---

1. The problem has been summed up in a similar instance as in the final analysis, one of organisation.—*Eastern Economist*, 7th October, 1949, Page 529.



ensure the increase sought later. There are certain spheres of economic activity in which quick results must not be expected—and this, we are sure, is one.

### **Research**

A word may be said about research and the timing of industry in relation to other development. We have seen that industry is necessary to draw labour which a reorganisation of agriculture will release; and that increasing incomes in one sector must be matched by increasing incomes in the other sectors if development is to proceed successfully. We have also seen that, in the absence of sufficient steady export income, certain import substituting industries are essential. Whether new export income will become available in amounts required for full employment was considered highly doubtful; in any case, it is unascertainable till after several years or decades. Their profitability being as vaguely known as that of import substituting industries, there is no case for special emphasis on them now at the expense of the latter which fulfil a purpose as 'basic' industries. The sounder policy would be, having investigated the costing, location and other possibilities of the wage-goods industries to invest on them. Simultaneously in the program, an active scheme of research on potential exports (through small scale manufacture or large) should be inaugurated. But in any planned development it would be a mistake to neglect industrial investment while agricultural development is under way, and concentrate only on industrial research.

### **Domestic Industries**

We now come to the sector of the economy covered by domestic industries, that is industries that are neither export nor import-substituting. As we saw, they must, consistent with social and physiological requirements, await satisfactory diversification of the economy based on industries replacing imports and on exports. There are certain items like housing and minimum rail and road building activity, which certainly must exist. The case for buildings and for works, merely to maintain incomes, has no place. Even the housing and so on must needs proceed simultaneously with investment in agriculture and industry, and can by no means be isolated. It is unfortunate but true that social considerations which



a richer country may be able to highlight cannot be so treated by us at this stage. While a minimum is necessary both socially and for reasons associated with productivity, that minimum quota must be quid pro quo for productivity. Among the items under Social security, old age and similar disabilities have of necessity to depend on more income for solution. But the problem of unemployment assurance and relief payment entails very different considerations in this country. Barring a case for this during frictional unemployment (which presumes the existence of real employment, that is full time industries employing the population), there is no case at all for introducing 'allowances'. The situation in Ceylon is one of unemployment (and under-employment) that is neither temporary nor cyclical nor sectional but permanent. The immediate problem is not to provide allowances but to create true employment. In this, the allowances can play a hitherto little emphasised role; that we shall consider very soon in the next chapter.

Once the desired economic set-up is introduced and is on a firm enough footing, there is then ground to expand domestic industries—for maximum domestic welfare—to the maximum limits. The sacrifice is one of giving up consumption now for purposes of more consumption, and more lasting consumption, later on. At present we fear that the roles are sometimes being reversed and the latter is being introduced with little or none of the former in existence.

### Summary

We may condense the policy for full employment as outlined in this chapter, into the following framework :—

- (1) The basic industries are wage-goods industries.
- (2) Full Employment must be sought by planned development (rationalisation and investment) and not by any adjustment, however clever, within the existing framework.
- (3) Both farm and factory must come in and at a relatively high level of co-ordination between them.<sup>1</sup> The pattern

---

1. The point has been observed in other Studies in much the same manner. e.g. Mukherjee in the Foreword to T.R. Sharma 'Location of Industries in India' speaks of the lack of liaison between agriculture and industry (Page IX) and Sharma observes in Russia the obliteration by Development of the difference between agricultural and industrial regions in the sense that not only are there



will be one equally of small or 'cottage' and large-scale units. Development must cover Wage-Goods industries, feasible export industries and ancillary industries in the tertiary sector as well as feasible small-scale machine manufactures required in the agricultural and industrial units contemplated.

- (4) The process of development must be by elimination of all 'surplus' at every stage; the constant objective must be creating of optimum combinations all along the line ( and not being satisfied with sluggish activity like 'public works') till final full employment is thereby attained.<sup>1</sup>
- (5) Among the Institutions required for this are a Body for Planning, a Financial Body with sufficient funds independence and courage to transform the economy, a Body (of wide competence) for technical Assessments, and a Body for Research.

---

modern industrial towns but the villages are also modernised, in regard to forms of production, nature and amount of output etc. Also c.f. W. A. Lewis 'An Economic Plan for Jamaica' (Agenda November, 1944) talking of fitting industry into the seasonal rhythms of agriculture.

1. It is interesting to compare Russia on the eve of Development. "Administrative reorganisation resulted in a drastic reduction in the numbers employed on the railways; the number of administrative workers in the textile industry was reduced by a third and the number of productive workers per 1,000 spindles in operation was halved.... The first accompaniment of reconstruction was, accordingly, an increase in unemployment." Dobb, Page 152. It may also be interesting to note that the 'fundamental and decisive economic task' of the Second Plan was defined as "the completion of technical reconstruction in the whole of National Economy". Dobb, Page 269 quoting from the Plan. By way of interest, some indices of Russian economy after development, may be mentioned. In 1939, the annual traffic per mile of track (traffic co-efficient) was more than double the figure for the U. S. (Of course the smaller total mileage explained a considerable amount of this increase). Another measure was that over the two Plans the amount of mechanical power per worker had grown at a mean annual rate that was more than double the annual rate of growth of power per worker in the industries of U. S. A. between 1899 and 1929. Again, "the U. S. S. R. had become the largest producer of tractors and railway locomotives in the world, and the second largest producer of oil and gold and phosphates." Dobb, Pages 273, 280. Between 1926-1939 "the rural population had declined by 5% (and the actual farm population by considerably more) despite a national increase for the whole country of 15.9%; while the urban population had doubled,"—of which some 20 million was by migration from the village. Page 285.



It will be reasonable to expect (a) a rapid expansion in employment in the secondary and tertiary sectors, and (b) a more or less uniform increase in productivity per worker in all sectors. In view of (a) however the *rate* of expansion in agricultural output will not probably be as high as in other sectors. This is generally borne out by experience elsewhere. It was so in Japan. It has been evident also in the economic statistics of the United States over the first four decades or so of the Century.<sup>1</sup>

In Japan, employment in Agriculture remained stable between 1920 and 1935, while the increases were in other sectors, especially Manufacturing, Commerce and Public Services and Professions. Total output in agriculture rose from 28.6 in 1873 to 109.5 in 1927 and 125.7 in 1933 (1921-5=100), though generally ranging in the latter years between 100 and 110. Industrial production rose from about 20 in 1907 (estimate) to 167 in 1937 (1931-3=100).

In the U. S. A. between 1900 and 1940 (a) there was a decline in employment in agriculture of 18%, and an increase in Manufacturing of 92%, Other Industries 29%, Mining 37%, and Public Utilities 105%, (b) there was a decrease in employment per unit of product (i.e. increase in product per worker) of 48% in Agriculture, 50% in Manufacturing (1899-1939), 61% in Mining (1902—1939), and 50% in Public Utilities (1899—1939), (c) expansion in agricultural output (1900—1939) was 60%, Manufacturing 267%, Mining 240%, and Public Utilities (1899—1939) 310%.

International trade and international problems will be taken up in a subsequent chapter. Here we may briefly mention the trade pattern that will correspond to full employment in the agricultural country. The entire range of important food-stuffs (grain, pulses, fish, meat supplies, sugar) and the major part of ordinary clothing as well as some silks will cease to appear in the import lists; so also several items like fertilizers, cement, bottles and so on and several leather and rubber goods; but not, we think, most of the other consumer goods (which includes items like cutlery, crockery, certain books and so on. On the other side, the import of certain tools and of machinery and allied goods is bound to be conspicuously

1. Vide Allen *ibid.* Appendix B, Tables III, IX, and XIII; and T. W. Schultz 'Changes in Economic Structure Affecting American Agriculture' (*Journal of Farm Economics*, 1946, pages 17 & 18).



larger. In internal distribution, the wage goods will, of course, play a correspondingly larger part, and also items like dairy produce fertilizers, cement and handicrafts. The export category will still be largely dominated by present items, but increasing shares will be registered by several processed goods and spirits and the like, by handicrafts, by some new agricultural commodities, like fish, cotton, cinnamon, and by an increase in tourist income. There is nothing new in this statement—it is merely a reflection of the production programme envisaged. However, it brings out in relief not only the increased output but the stability of a new situation that will raise the standard of living and provide the proper basis for the functioning of the social services State. An overwhelming import percentage of agricultural products is a dangerous factor and needs to be overcome—either by substitution of home activity, or by converting the economy into a dominant industrial country, or some combination of both. In the case of Ceylon, it will largely be the first solution, in the case of India the last. Import volume will still be maintained, but it will not be the present imports. The question of balancing the payments itself is no problem as such. Ceylon, for all its precariousness through fluctuations in foreign trade, had an adverse balance only in 1932 and 1947 in the 25 years ended 1951. The problem is one of balancing at a given level. That given level must be determined now by the required standard of living and later by raising the standard with increasing prosperity. So, the significance of import volumes will remain. But they will not dominate the economic trends within the country as they do now.

The transformation effected in Denmark by industrial development is an interesting epilogue to this chapter. Danish activity now covers a wide range of commodities. It has a large food and drink industry. It also “processes imported raw materials fully, meets the Danish consumption requirements of industrially processed goods and leaves a considerable balance for exports.”<sup>1</sup> A large fertilizer industry has accompanied the growth of the highly developed agriculture. About two-thirds of the home consumption of textiles is covered by home industry. The boot and shoe industry meets the bulk of the internal demand. The biggest is the iron and steel industry which includes engineering, electro-machines,

---

1. Eastern Economist, January 20th, 1950, Page 102.



ship-building and the manufacture of the means of communication. There are also paper mills and rubber factories, oil and soap mills, paint and varnish works and many factories which make chemical and pharmaceutical goods, besides cement and porcelain works. Before the war, two-thirds of the internal consumption of industrial goods was supplied by the home industry, which occupies an important place in exports as well. The share of mill goods was 25-30% of the total exports.



## CHAPTER ELEVEN

# Policy for Full Employment

## HIGH-COST INDUSTRY, FISCAL POLICY AND SOCIAL SECURITY

### Question of High-Costs

THROUGHOUT history, the start of economic development in a country has involved competitive price disabilities vis-a-vis the more advanced countries. The infant industry argument was a reflection of that position. It was implicit that the argument was valid only at the infant stage and that, in the end, the old-time principles of comparative cost will prevail and will be vindicated by the competitive cost of production. This involves a clear policy on protection. We do not pursue that immediately, however, but shall consider a neglected, but crucial aspect of this question first. While we do not expect that the problem will arise as a general feature, the likelihood has to be faced of some industries running at a loss, if called on to produce at competitive prices. We refer thereby not to a temporary but to a quasi-permanent feature. It is not impossible that rice cultivation as well as, say, trawler fishing (if the industry is capitalised at present prices of capital equipment) may have to be run 'indefinitely' at a loss or without normal profit. The dilemma will arise out of the tussle between absence of economic feasibility and presence of perfect favourableness technically. We have already seen the need for basic industries for final full employment. Keeping that in mind, we shall develop the argument further to show that the running of certain industries, even at some loss, constitutes a direct economic gain and is economically sound and imperative.<sup>1</sup> "Suppose there is full employment, the 'surplus' having been absorbed by the new industries started. Now according to the laissez-faire argument, if goods coming from abroad are cheaper than similar ones made at home, then the home industries should be closed down and all would benefit. In other words, we must dismiss the labour in the industries. Now it is expected that the labour thus released will go to increase production of those

1. Adopted from my "Ceylon, Beveridge and Bretton Woods", Pages 40-1.



commodities in which we have a comparative advantage over other countries. These, for us, are tea, rubber and coconut. Already however, we have seen that an economy based on such industries does not merely register a fluctuating national income, but also that the income so derived will be less than if the home country had equal bargaining power with others. This can be only if the former does not depend on its imports for its necessaries. To add to this, if the dismissed labour is brought on to a production of these stock commodities, the result can only be a disastrous deterioration in total revenue and standard of living. It seems conclusive that employment in the present industries must be considered out of the question. But faced with the no less distasteful alternative that in respect of the other produce, the 'local' costs are higher than those of the imported,<sup>1</sup> the Government has not found room to be bold enough. It was partly to be expected: for the issues should have been put differently. The question before us should be and is whether employment in (these) other lines is better than no employment at all. And that is a deciding question. If it could be seen that I cannot pay by corresponding effort for a good which I want and which the other fellow makes for me in one hour; if indeed I cannot pay even by working two hours, but can only make things worse thereby, in stuffing him with the only thing I can make (e.g. rubber) and accumulating debt and never catching up; then the only thing to do is for me not to remain idle for I have time to spare (c.f. the under-employment or disguised unemployment) but to stop taking from him and to spend the two hours in making for myself that thing I want (on which he spent only one hour, admittedly). I should be able to better my prospects both in respect of my revenue from "rubber" and in respect of my standard of living. Instead of that, we are often confirmed in the "sanity" of remaining 'idle' while begging from the third fellow (e.g. the policy of unemployment allowances). So put, the whole position may not appear to most people to contain anything objectionable. But when we say the same thing in other words, viz, that we uphold and recommend the running of certain industries at a loss the suggestion is all too likely to be dismissed. In other words, we will not

---

1. The argument has been raised that stopping imports and installing internal industries raises cost of living. It may be remembered however that any of the other solutions too, of devaluation, lowering of wages etc. does the same. Besides standard of living is different from cost of living, and under the first device the former is most likely to improve. c.f. Lewis in Agenda, November, 19, 1944.



have anything to do with desirable ventures that are only partly wasteful, but will cheerfully encourage those (c.f. relief payments, allowances etc.) that must be considered wholly wasteful indeed."<sup>1</sup>

### Validity of Protection

This line of logical reasoning does not, of course, answer the question as to the particular method or methods by which high-cost industry is to be kept going. There is need for proper policy judgement on this point. The relevant problems are not different from those arising in regard to the more normally understood infant industries. We may well consider both together from now on.

We are concerned with the propriety of a policy of protection and with the nature of that protection. The case for protection, in so far as essential industries are concerned, is covered by the argument for the high-cost industry. Now, however, it is useful to view the question from the more broad-based point of view.<sup>2</sup> "The question is certainly involved and may not be dismissed off hand. To argue first in general terms (with no particular local reference)...we are told, in defence of free trade, that prevention of imports of one commodity will mean reduction in the purchasing power made available to the foreign country with which to buy the exports of the home country, and thus a disorganisation of the flow in world trade, with the foreign country reducing its own imports, and the home country having to reduce its imports still more and so on. (However, there is a quiet negligence of the fact that the free trade argument can be true only on the assumptions that, over a period, there is full employment in all countries, and that the balances of payments are always even)...On the other hand, protection would argue that a barrier on one commodity coming from outside will mean employment to the corresponding trade within the country, and that in addition the hands so employed will also provide the market for those goods which hitherto went out in payment of the goods now supplied by the newly employed at home.

1. Incidentally, c.f. Swatantra, February 12th, 1949, Page 6—"We spent 5 crores to obtain 7 tons of foodstuffs, or about 7 crores for a million tons of foodstuffs. This compares very favourably with spending nearly 50 to 60 crores or so during the last year in importing 4 to 5 million tons of food grains from abroad. These figures work out to an average of about 10 crores for a million tons—nearly one and a half times the cost of raising the same amount of food at home."

2. My "Ceylon, Beveridge and Bretton Woods", Pages 36-7.



The case of rubber in Ceylon can be an apt illustration. It will of course, correctly be argued that the whole of the raw material like rubber or coconut cannot be used within, and that still the question of export will remain. As partial contradiction, it may be shown probably that the conditions of demand for goods like tea and rubber and also coconut are such that a given quantity will be demanded irrespective of the amounts imported (e.g. by Ceylon etc.) in return. Besides protection is on surer grounds in countries like Ceylon (as opposed to say Britain) because (while protection in the latter will not avail for the reason that its difficulties have been not really competition in its own market, but in foreign markets with other competing countries) in the case of ourselves, prevention of goods into the country must be with the purpose directly of ensuring the home market for home industries, and not for the generally uneconomic idea of competition of home industries in markets abroad. In a sense, however, all this traditional method of approaching the question of protection is irrelevant."

As noted, the free trade argument is valid only in the absence of fundamental dis-equilibrium in the balance of payments. Under different circumstances, the argument is patently absurd and so is any claim that the free trade argument has never been properly answered. If applied in reference to a country showing ample surpluses in the payments, there is likely to be truth. A position where agricultural countries suffer continuing and additional imports in the face of simultaneous inability to improve on, even to maintain the old volume of total income or revenue, is certainly not a case where the free trade argument is valid. The implication of a free trade argument in these circumstances would be an attempt to have it both ways—for the more fortunate countries to have a right to export the maximum and to import, in the actual result, the minimum. Precisely the reverse should be the case; that is the lesson of all the attempts to establish an International currency with whose problems the point we are discussing now has much in common. In the final solution of the currency question in the field of international economic relations, the two indispensable constituents are sound planning and rational organisation of the economic structures of the countries, and the assumption by the surplus countries of a special responsibility to increase imports.<sup>1</sup> If that is

---

1. c.f. *ibid.*, Page 9.



to mean anything in the present context it is that the surplus countries must be ready to grant that attempt by others to balance their adverse payments (or payments favourable only on the basis of a very poor standard of living) is not a blow on the continuance of increasing trade; but that the real threat to buoyancy is in the accumulation of surpluses by countries not importing enough.

The absence of protection, by fattening the surpluses of net exporters, lends disaster to deficit countries. Protection by the latter cannot carry the same consequences to the creditor countries, but only lessen the surpluses accumulating and eating into the other economies. The case is different where surpluses are on Capital account and we shall deal with that in a later chapter; our reference here is to chronic deficits. Capital imports, if properly based, are far from indicating such characteristics. Chronic deficits on any account are clearly a matter where the free trade argument can no longer apply and even capital development may need to be financed at an added sacrifice by internal finances. By protection, therefore, is meant not discrimination or a form of War, but planning for a workable equilibrium. It is a piece of economic logic which one thinks is more inexorable than most of the other so-called laws of economic science. The very fact of industrialisation means a cutting off of the imports that had hitherto come in, and the real answer of the surplus countries should be not protection in return but suitable adjustment of their structure to meet the new import demand of the former deficit countries. It is in the individual interest of every country as well as in the larger world interest. So that if the free trader says that protection is bad because it will reduce imports by other countries as well, we may say that (besides the argument's other flaws) it is irrelevant.

“Even under free trade, we should expect, for the end of altering the structure of our economy, a reduction of imports immediately on the creation of certain ‘essential’ industries within the country. It is the responsibility of the ‘surplus’ countries, (it is, also, as we saw, to their advantage in the given economic dispensation) to increase exports different from those they hitherto sent out. For example, light machines could be exported. It will, of course, not serve the interests of the importing country to barricade them. To protect the economy we must ‘industrialise’; to industrialise we must ‘protect’”.....



"All that we need know is that if it is not possible for the required (as to really what are required, we must go back once more to the previous chapters) local products to keep out the imported without any aid, then they must be enabled to do so by means of enlightened intervention. Besides, when we have given up unrestrained free enterprise in favour of a method of planning, of ordering of the system from a centrally constituted source, free trade as such goes automatically. In planning, protection is already contained. The creating simultaneously of a 'complementary series of industries' (agricultural and industrial) may very probably entail the necessity to give special support to some in order to prevent their falling to ground as a result of foreign competition."<sup>1</sup>

### Measures for Protection

We have now to analyse the nature of the protection to be recommended. It must be noted that the measures for protection to be recommended relate to the protecting of the economy in a comprehensive planned programme and not to a 'laissez-faire' approach. The consequences of particular measures could well be different in the two varying backgrounds. We do not need to go too much into the various protectionist devices. Exchange Controls, Bilateral Agreements and similar measures so profusely tried in the thirties and existing today are all quantitative restrictions and so measures for protection. Quotas have been named a half-way house between a liberal and centrally planned trading system.<sup>2</sup> We may, for brevity, use this as a compendious term to describe all quantitative restrictions. Quotas, quite naturally, were more favoured, the greater the general monetary instability. The context for such instability is generally more prevalent when the concomitant problem is one of balance of payments difficulties. To that extent and especially in the present situation of the agricultural countries, quantitative control dominates the scene and is bound to remain. Within this framework of planned trade, however, there are other important issues at stake and remaining to be decided correctly. For within the planned volume of trade, there are several items that go to make up this trade. The possibility of different ways of affording protection to new production is

---

1. *ibid.*, Page 38.

2. *c.f.* League of Nations, "Quantitative Trade Restrictions."



certainly there. In other words, in addition to the protection to the economy in general, there is also protection to individual units of production within.

Reference has been made to the principle that given protection now the industries will be able to stand on their own in time. The principle is sound. We have seen it to be sound even if the higher costs are not to be completely made up in the foreseeable future. There is no case, however, for the conventional association with the infant industry argument of a policy of tariffs. Quotas and subsidies may as well be used. Tariffs once granted are noted to have a tendency not to be withdrawn and efforts may not be made to reduce costs to the competitive level. Quotas and subsidies do not, however, create the same expectation that they cannot be revised downwards easily or even withdrawn—though the reason may be nothing more than conventional or political. For example, 'quotas...are rarely fixed for a period of more than one year.'<sup>1</sup> Tariff changes generally go through legislatures and take more time. Historically the "Netherlands Government justified recourse to quotas on the ground that quotas were preferable to tariffs as an emergency measure; for it was assumed that they would be easier to abolish than duties after the depression had passed. Quantitative controls have been abolished in the 20's, but experience has generally shown that duties were hard to reduce after having been in force for a while, and instances of tariff reduction have been few and rare."<sup>2</sup> On the other hand, quotas are said to have a tendency to encourage monopolistic growth within. Tariffs have the advantage over quotas in that the level of the new prices is more precisely known, while quotas will leave the point vague. Yet, price rise under quotas is likely to be less. Besides, the fact of a definite quantitative restriction is thought to be more direct encouragement to internal activity than tariffs.

This is but a skeleton statement of the several arguments that can be brought into the field; even with the fullest presentation of facts we should not be inclined to make any clear decision in favour of one or the other on the basis of the foregoing lines of argument. In a country, however, whose level of incomes is generally low, we place more than ordinary emphasis on the virtues of preserving the

1. *ibid.*

2. *ibid.*, Page 32.



lowest level of prices, in relation to the given volume of money. In the present situation and equally in the process of development, it is important that at least the wage-goods should continue as low in price as possible. Tariffs will certainly lead to the contrary effect and, vis-a-vis quotas, will require a high rate to keep imports down to the quantities dictated by expected internal increases of production. The higher the internal cost of production, the higher the tariff has to be. Very high prices and cost of living will be the result.

Quotas would, of course, not bring revenue to the State unless accompanied by a system of exchange or licence sales. Subsidies hold similar disadvantages, but they contain the major argument that they promise the eminent advantage of maintaining prices of goods at the known world competitive level—which neither tariffs nor quotas can achieve. It may, indeed, not be possible to work fiscal policy on subsidies alone, but in so far as prices are a vital factor in the economy, subsidies should, without doubt, form a fundamental measure of protection in the programme of development.<sup>1</sup> For reasons connected with the efficiency of production and consumers' preferences, the imports may still find large markets. To that extent other measures of protection must come to the aid of the subsidies. A policy of quotas where the required tariffs would be too high and affect cost of living with tariffs in the other categories would be the basis on which to operate. The particular application of each method and even combination of methods (e.g. the tariff-quota) are really matters for decision on individual observation of each case,—its market trends, trends in purchasing power within and so on. What is important for us to bring out is the emphasis and preferences to be attached as between several types. In this respect, there is great room for change of ideas and for much more consideration to be accorded to subsidies which, far from being the fundamental method, is often relegated to the background.<sup>2</sup> Of course, just at the moment with world shortages of

1. Subsidies need not be solely in the form of aid to individual Units. Subsidising the basic services of a 'development area' is another method. This is recommended for instance by Lewis in connection with the setting up of trading estates. c.f. *Principles of Economic Planning*, page 79.

2. A favourite objection to the system is contained in the statement that subsidy "clogs the working of the pricing process." In point of fact it enables the pricing process to work in a situation where otherwise this very process will distort the set-up and bring the whole structure, including itself, down. c.f. W.A. Lewis, *Principles of Economic Planning*, page 14 "Only state action can assure competition."



production and so on, subsidies are performing a different function of reducing the prices of import goods. This situation would probably have to go on side by side with subsidies to internal produce (for example rice) till import prices come down to a more reasonable level, at which stage subsidies to internal production may still continue, in all likelihood at a lower rate.

Since subsidies involve adequate State revenue, tariffs, as we said, will form part of fiscal policy. A particular local product may be subsidised from a tariff on the corresponding imported variety ; or tariffs on selected goods may jointly be used for selected subsidisation. In the former category come several fiscal measures adopted by Japan in the thirties. One case was that of duties on imported oil so as to provide funds for subsidising of home production and for the development of hydrogenation.<sup>1</sup> Subsidies are meant for the basic industries. The case for it as a practical proposition rests on this as well as on the point that the difference between internal and external prices cannot be gaping. In actual reality, there may occur instances of wide difference in price. This likelihood is greater in the early stages. The treatment of such cases would call for judicious combination of the best and the most suited protectionist devices. Just the fact that the difference is gaping is no case for dropping of subsidies. For, without them and with tariffs alone the rise in prices will be phenomenal. It is precisely in such cases that subsidies should be used to the utmost reasonable limits. Tariffs should be brought in to cover really the residual difference. Subsidies also have the great advantage of being a far more sensible use of the present (and contemplated) disbursement of purchasing power (for social servicing and so on); but we shall come to that in a moment.

Meanwhile, we may illustrate the place of subsidies in protection policy with a recent concrete case that came up in India. On the recommendation of the Indian Tariff Board.<sup>2</sup> "The aluminium Industry in India has earned the singular distinction of enjoying the simultaneous benefit of an ad valorem duty, a specific duty and a liberal subsidy—factors which explain at once the nascent character of the industry and its basic importance to the country." The

1. G. C. Allen. *Ibid*, page 147.

2. *Eastern Economist*, June 24th 1949.



supplies of bauxite, the principal raw material are both plentiful and of admittedly high quality. "The total demand for aluminium products in the course of the next three years has been placed at 20,000 tons per year, out of which 7,400 tons at the most can be produced during this period by the two existing units. It leaves a wide gap of 12,600 tons which can be bridged currently by imports but eventually by expansion of the home industry." The country is relatively very poor in all other non-ferrous metals, and aluminium alone can fill the void. "The criterion for fixing the quantum of assistance is an assumed fair selling price for the products of the two Indian units, as based on their costs of production in relation to the fair selling price of similar imported products. The computations are based on the landed cost, the ex-duty of aluminium being Rs. 1,275 per ton and that of 20 gauge circles being Rs. 2,614 per ton. It is clear that the rates of duty and subsidy are liable to readjustment in case there are appreciable variations in the prices of the imported articles." The device of triple assistance becomes essential in the face of the gulf between the prices of the home and imported products, which was "so wide that not even a 100% protective duty would have sufficed to cover it."<sup>1</sup>

In the proposed policy there is a downward scale for the assistance recommended and the scheme is for an initial period of three years only. "The rates of subsidy are fixed at different scales in the case of the two units after careful consideration of the differential nature of costs of production reflecting the stage of efficiency attained." The rates themselves are estimated on the basis of assumed reasonable costs of production.<sup>2</sup>

---

1. c. f. *Eastern Economist*, November 12th, 1948, Page 832. Some figures collected by the Chloride Electrical Storage Coy. (a subsidiary of the U. K. firm) of comparative labour costs in their Manchester and Calcutta factories are arresting. While 22 workers in the assembly section of the Manchester factory turn out 2,000 batteries a day, 30 workers in the corresponding section of the Calcutta factory produce only 300 batteries a day. So that even allowing for the wage rate being only a quarter of the Manchester factory, labour cost in Calcutta is more than double that in Manchester.

2. *Eastern Economist*, November 12th, 1948, Page 831. The report of the Tariff Board on the motor battery industry is another interesting case. In making its recommendation the Board "based its estimate of fair selling prices of the indigenous product on a number of liberal calculations and allowances of which a margin of 20% to overcome consumer preference for the imported product is the most outstanding.



It is implicit in such a Scheme that no effective scheme of assistance and no planned development in the economy is possible without the presence of certain technical abilities in organisation and operation of Units. On the part of the State, there is need for statistical, engineering and costing experts. Absence of these could result in under-assistance to some or all of the Units and therefore, likely failure; or over-payment resulting in wasteful and costly financial burdens to the country.

The following would illustrate the type of questions involved. "The Aluminium Corporation of India, a purely Indian concern, has made a judicious choice in selecting location for its Plant. Its works are situated at Jayaka-Nagar near Asansol in the West of Bengal in the vicinity of its own coal mines. The Corporation has its own Bauxite deposits at a distance of 170 miles from the Works. It generates electricity from coal at the site of the Works and its entire manufacturing Plant in this way is concentrated in one place. Its alumina Plant, the smelter, a small rolling mill and power house are in the same premises. The total capacity of the reduction works is 2,000 tons per annum while the capacity of the alumina works is 6,000 tons per annum. This is a case of clear unbalance, because on the assumption that two tons of alumina are required for the production of one ton of aluminium, the plant has a surplus capacity of 1,000 tons per annum for which there is no market at present. It is possible that one major cause which explains the high cost structure of the Corporation, is that the reduction works do not operate at full capacity. Power is also generated at comparatively high cost. The unbalanced nature of the Corporation's plant is said to be explained by the fact that orders for it were placed on three different fabricators. There is generally a lack of proper technical direction. The Board finds it difficult to exonerate the management of the Corporation from the failure to place orders for some missing links in the Plant and cites the instance of the omission to acquire the third boiler necessary to operate the Plant at full capacity. It has made the pertinent recommendation that as a condition precedent to the granting of subsidy the Corporation should be required to appoint on the Board of Directors a Technical Director who should be a person with experience of the production of aluminium and not as at present a person who never worked in an aluminium factory."



The Indian Aluminium Company, (still considerably managed and controlled by British and Canadian hands) having its rolling mills at Calcutta "have a capacity of 1,600 tons per year consisting mainly of sheets and circles. Its reduction works are situated at Alwaye in Travancore State and are run with the active assistance of the State Government. Their capacity is 5,000 tons of ingots per year. The projected alumina works with a capacity of 10,000 tons per annum are under construction at Mur in Bihar. Alwaye was selected as the site of the smelter as cheap electric power was available only there. But the problem before the Company is to obtain yet cheaper power which is possible from the Travancore hydro-electric scheme. It has been reckoned that for every ton of aluminium produced nine ton-miles of raw materials and semi-manufactured goods have to be transported by rail. The burden of transport, cost, which is already heavy for the industry is further increased by high freight charges on Indian Railways. The Government is considering the question of concession in railway rates. Since the alumina works will be situated in Bihar, the most rational and practical solution for the Company will be to shift its rolling mills from Calcutta to Alwaye."

On the long term prospects, the position has been outlined thus; "Pre-War aluminium industry was controlled by an international cartel which was dissolved during the War with no chances of revival now. Competition on the basis of price reduction, promises to be fierce in the future and in the meanwhile improvements in production techniques will continue to be registered. The prospect at the end of the three-year period will not be free from vexed problems and the indigenous industry can hardly be expected to outgrow its infant stature within this span."

These are indications of the nature of our problem. They also indicate the need, if we are to succeed in the long run, to decide in the context of the larger economic background, and not to be confined to the immediate 'commercial' nature or otherwise alone of the Unit. The discussion in this chapter seems to emphasise the outstanding importance of fiscal policy in the attainment of successful employment level. If the cost of the subsidy is met from the returns of duty on the imported article the subsidy effects a double economy, more noticeable where 'gaps' are wide. It would



cover, with a given quantity of money, a 'gap' for which double that amount would be required if the dependence were on subsidies alone, and cover double the gap than if the dependence were on the tariff alone.<sup>1</sup>

Before we leave this subject, we must refer to one more point. A mere quota or even subsidy (or subsidy-cum-tariff) does not thereby imply automatic sale of local output, especially the entire output. While subsidy continues to remain the basis for protection, where import goods normally flood in (and probably sell on mere consumers' preference) the determination of an import quota together with the condition attached of purchase of a stated amount of the local equivalent, is the nearest to a fool-proof system. It is an ideal method for most industrial products assuming a minimum standard in them (and for agricultural produce too if the present world shortage suddenly turns into a surplus and consumers' preferences are strongly for the imported varieties). The device must not be permanent, and should further be reviewed from time to time for adjusting of ratios, raising of local standards required and so on. To start with itself, the local products should first conform to a standard before they could be extended the protection of this device; for example a Standard like that in the local cement produced from the recently established factory. Allowing sub-standard products in the market is unfair both to consumers and to the traders.

This is the principle underlying the Industrial Products Bill which was on the anvil at the 1949 talks in Annecy, France. The reason before the ITO was that it is tariff policy in another form and contrary to the principles of progressive tariff reduction envisaged by that body. It is wise not to deny that, for though technically it constitutes no limit on quantity of imports, in practice it does. It is, yet, unfair to overlook the point that it is chiefly a marketing device and the 'tariffs' part proper is in whatever subsidies-cum-tariff-policy that may be superimposed on it. However, all this is only a nebulous way, at best, of vindicating the position for the Bill.

1. A similar interesting analysis appears in the Eastern Economist of February 17th 1950, Pages 246-7 on the optimum size for steel. The combination in India, of the highest ore content of 60 to 69% (equalling that of Brazil and South Africa and better than Australia) and inadequate skilled labour and present high costs of capital goods, contributes to make the analysis certainly a typical one for a Planning Body.



The central argument for it is precisely the same as that detailed in stating our case for protection for the high cost industry. If the country cannot afford imports beyond its capacity for exports, it has to solve its problem of the standard of living, not by attempts to balance its payment at a higher level than it possibly can, but by balancing at the appropriate maximum level and adding to national income by internal production. The ITO does in fact recognise special rights to protection by under-developed countries and so long as unconscionable use is not made by mis-use of the advantage, the principle underlying it must be conceded to be fundamentally both sound and fair. It may be noted that a fair use would most probably be indicated by confinement of these measures largely to what we have defined as basic industries. Finally, it may be said in passing that it is precisely such measures as envisaged in the Industrial Products Bill that the U.S.A. used for its synthetic rubber industry and with much less economic argument.<sup>1</sup>

### Fiscal Policy and Social Security

There is also a very important sense in which subsidies will play a crucial role in the economy and to which we made passing reference a little earlier. We have seen more than once, in the previous chapters, that the means to final full employment is really an industrial policy and not employment policy as commonly understood. We have already seen that the running of *certain* industries, even at a high cost, is not an economic loss and is on the contrary a net gain to the economy. It would not appear to need much explanation now if we say that the subsidies paid do not even constitute any monetary burden to the State beyond that already contemplated in a policy of Social Insurance, Unemployment Allowances, and similar payments. In other words, the Industrial policy incorporates Employment policy in yet a new sense. Subsidy has the property of fitting in ideally into a planned system. Almost automatically, it combines within itself the function of an instrument of protection for an industrial policy as well as the function of an

---

1. Above all there is the Buy American Act of 1933. In respect of total purchases in the neighbourhood of \$10 billions per annum, for which the Federal State and Local Governments are responsible, every purchasing authority in the U. S. has broadly to satisfy itself, before a purchase from a foreign source is made, that a product of local origin would cost more than 25% extra if the purchase involves more than \$100, or more than 100% extra if the purchase involves \$100 or less. Eastern Economist, January 6th, 1950, Page 15.



ideal weapon, under modern employment policy, for subsidising purchasing power. The point is that in the absence of the new Units inaugurated, labour is permanently without purchasing power and the State will necessarily involve itself in certain commitments by way of relief and other services and allowances. This fund, disposed of as subsidy, would represent, if properly grasped, not a dead-weight but a measure of the State's reserves of strength that could be utilised to prop up a development programme. For, the institution of industrial units (broadly speaking) automatically implies transference of the idle labour into a new set of circumstances, and 'relief' disbursements hitherto borne by the State do become to that extent an immediate subsidy to the new industries. "Subsidies have to be paid only to the extent of the margin between the home costs and 'competitive costs' and in doing so we should feel that the commitments will be less than those entailed in paying as allowances what the unemployed man will need to keep him decently living. (Of course, even if it were more we have seen that the position of the status quo plus allowances cannot be continued without inviting deficits and probable bankruptcy.)" In the case of allowances, "having given the purchasing power to the population (even granted that it will not be less than the rates of the wages to the employed) we have still to import the wage-goods and that (in the absence of subsidies and prevalence of tariffs) at high prices; but with subsidies, we have created the goods and also handed greater purchasing power (wages and subsidies) to the poorer sections of the population. Thus, instead of higher prices and less additional purchasing power, we substitute world (lower) prices and 'more' additional purchasing power. We have, besides, left the corresponding balance in imports (plus that from the gain through better 'terms' for the 'old' industries) for importing needed equipment and the like and for bettering the standard of living."<sup>1</sup> It is the intimate association of these new industries with labour that would otherwise have been considered unemployed, that is the key point. Subsidies are nothing else but just unemployment allowances, not for idling but for producing. And so in this respect too "we need no longer talk of an 'employment' policy separate and an Industrial Policy separate, but that subsidies are the allowances etc., (administered in a much better way); and we may omit the misleading terms like relief and

---

1. c.f. My "Ceylon, Beveridge and Bretton Woods", Page 42.



allowance and rightly call all, subsidies to industry, (in which term we also confidently include such things as road-making and so on) the entire activity contributing in the most economic manner, to a raising of the standard of living."

The first Annual Report of the Monetary Board of the Central Bank of Ceylon devoted some space to the subject of subsidies.<sup>1</sup> The chief concern of the Report was with the relevance of subsidies in an inflationary situation. In the Report, Subsidies have been strongly condemned for the most part. Their role in a normal situation, or as a fiscal agent in development policy is not apparently considered in arriving at the judgments. The arguments adduced therefore must, if valid, be considered to be only of limited validity.

The subsidy talked of in the Report is chiefly for consumption goods imported at high cost. The subsidy advocated in this thesis refers to local manufactures competing with their cheaper imported counterparts. The 'alternatives' discussed by us have been Tariffs or Subsidies. The alternatives discussed in the Report are cost of living Allowances or Subsidies. The latter set has no relevance to Economic Development, but is confined to discussing inflation in a stationary economy.

After some peregrination the Report almost explicitly comes near this point. Implying that whatever measures it suggests are not ultimately sound for the economy, it adds that "the surest and most effective cure in an inflationary situation is an increased supply of goods." It further adds "It is obviously to our advantage to emphasize the contribution made by domestic production." It is a matter for some surprise that there is hardly any recognition of these objectives in the judgments made on subsidies. Not subsidies (we are not endorsing the actual rate) but the failure to inaugurate, simultaneously with them, a planned program of productive Investment should be the feature isolated for criticism in the present Scheme of Subsidisation. It could well be recommended, theoretically, that subsidies be stopped or modified according as a production program is not being implemented or only partially implemented. Given such a program, however, it would be difficult to condemn subsidies out of hand.

---

1. c.f. The Report for 1950, especially paras 35-42.



Apart from the possible mistake of devaluation (on which we comment in the Chapter on Planning) the defect in Government policy has been that more use of the situation has not been made to put through a planned development programme; and that, in holding down prices of imports, the standard of reference must be what would seem normal world prices in the future state of normalcy and not (for instance) the pre-war price. There is also no reason, as the Report feels, why the employers should not meet the subsidies in regard to their employees in prosperous sectors (for example plantations). Subject to these, Government has acted wisely in keeping the cost of living down through subsidies, instead of sending it rocketing high even though it fully met it through cost of living allowances. The Government policy of subsidies has not been to the exclusion of cost of living allowances, nor of wages geared as far as practicable to the cost of living. Subsidies have held in check the more riotous effects of the rise in cost of living. The emphasis placed in the Bank Report on cost of living allowances and rising wages with rising cost of living, reduces to a pious wish the objective of an 'increased supply of goods'. In the present stage of economic development, a whole new economy is sought to be built on an inflationary price structure. A slight recession would be enough to convert the industries into ventures either heavily propped up or given up by a Government itself facing a 'thin' time. It would be a great gain for development if as many as possible of the input items for firms are not financed at 'inflationary' prices. Subsidies if we may say so, 'depress' prices now, without inviting a big depression later to do it. The 1952 Report of the Colombo Plan Consultative Committee on Economic Development refers to the effect of inflationary prices on development. "The increased cost of living was accompanied by a general increase in local wages, especially in the construction industries where the demand for workers increased owing to development programmes". As such "the cost of development increased".<sup>1</sup>

The effects of capitalisation at high-cost have been noticed in the history of all industrialising countries. One such case was that of Japan. The war-time boom went on till 1920 when the Index number of wholesale prices (base year-1913) stood at 322. It fell to 190 in August 1923, but with the earthquake of that year, a

1. Page 19 (Colombo, April 1952) c.f. also, in this connection, Page 98, para. 1, above



'reconstruction boom', under Government inspiration, sent the index to 214 at the end of 1924. Government disquiet and international factors led finally to the financial crisis of 1927. Several undertakings had come up during the war-time boom. The crisis of 1927 has been described as "of great importance for the future economic development of Japan."<sup>1</sup>

The reason given is that the unsound industrial and trading concerns were weeded out, or passed, "after decapitalisation" under new and more efficient control. It meant that a new net work of capital costs came into existence, that assured future stability in development.

Amidst all this, let us, however, not forget that Social Services proper refer to provision against a vast range of contingencies and for several needs—relief against unemployment and serious under-employment, sickness, unforeseen causes of expenditure, maternity and old-age, education. Subsidies, of course, cannot be considered a direct substitute for old-age and maternity provision, but they eliminate the need for relief of idleness as such and possibly enable the retired to draw something from the Industries on Provident Fund basis. The marked rise in incomes that an industrial policy, with the aid of subsidies, will register would itself enable a poor country to go slower in its obligation to provide for all the social needs of the population. But it is clear that no programme of social security of any progressive nature is feasible in the under-developed economy while the bases on which this can at all be built stand neglected. The so-called contributory advantages (through strengthening purchasing power) of a Beveridge Plan are all irrelevant in the context referred to here. Financially speaking, it is first necessary to create employment before we could relieve unemployment. If there is any significant argument in the British social security scheme for us, it is the statement that the national income is sufficient to make want unnecessary; social security is a distributive device. In a context where the minority has to pay for the majority, the conditions for implementation of such a scheme are certainly not there. Insistence on such can only lead to economic

---

1. G. C. Allen—Ibid page 96.



embarrassment, even to serious embarrassment both in regard to the balance of payments and internal debt.<sup>1</sup> Merely to create full employment by an industrial policy is admittedly not a complete objective. But in order that a State may fulfil its more eminent obligations the latter must be considered essential to the former. There is no easy cut to the correct economic solution. Services will have to develop only to the extent warranted by the success achieved in the industrial policy. It is not implied that very item of social security should wait long, chronologically; social security could well be considered simultaneously in point of time but later in point of importance. The scheme should be carried as far as but only as far as the larger purposes of economic policy would permit, and introduced also in a manner such as these larger purposes will allow. No better start could be contemplated for an advance on social security in these countries, than a welding of subsidies into an industrial policy.

---

1. c.f. Lewis on Jamaica (Agenda November, 1944) discussing the implications of British 'development' policy—that the 'present schemes' will end up in a structure of social services beyond their capacity to meet from their own resources.



## CHAPTER TWELVE

# Policy for Full Employment

### PLANNING

#### Its Fundamental Nature

IT would be wrong, even if it were not unjust, to maintain that the concepts of full employment and devices to ensure it emerged only with post 'classical' economics. The Theory of the 'unseen hand' was the first attempt and the rate of interest the most important in classical theory to accept a high and stable level of employment as a fundamental ethical objective. The increasing significance allowed to the rate of interest (and related credit controls), calling as it did for increasingly intimate knowledge of the various features of the economy and the forces working in it, constituted a measure of planned interference, the aim of which was certainly full employment. Keynesian theory re-wrote several of the fundamental concepts which some classicists and the neo-classicists had underwritten, and the result was the "full employment devices" as we know them today. It called not only for far more co-ordinated knowledge of the functioning of the economic system, but also for increased co-ordination in the sphere of conscious action towards full employment—in other words for planning of economic activity. Planning, then, is in any case fundamental to the achievement of full employment and it is as well to accept it once and for all.

However, the employment devices as normally understood are hardly relevant in the context of the economy we are analysing here. We have seen that economic development is a point of supreme consideration<sup>1</sup> and that an extraordinary measure of State intervention is required for the purpose. Planning must as such be appropriate to the requirements of these situations. The devices for full employment must be directly connected to actual investment and production in the economy; and even as planning out of the Keynesian full employment devices needs to be by the State, similarly, planning-out of the 'devices' here too will need to

---

1. "In early formulations of the Keynesian doctrines it was thought to be necessary to plan investment not to keep it high, but to keep it steady...." Lewis' *Principles of Economic Planning*, page 52.



be by the State. (It need hardly be said that this by no means implies that all Development must be State 'owned'—though certainly where other means fail the State must needs fill the gap.) This type of intervention brings us much closer to comprehensive overall planning than any cited so far. Planning is of course a concept quite opposite to that of laissez-faire and constitutes 'intelligent' interference with the economic system.

In the context of the advanced countries themselves, the planning necessitated involves advanced multi-angled and highly co-ordinated preparation. The calculation of various magnitudes like those of total income, capital formation and consumption on the one hand, and on the other simultaneous arrangement of due priorities for the objects of money disbursement, as well as treatment of the legal and administrative technical and engineering aspects of the problem—all these are sine qua non for a sound employment policy. In the less advanced countries, next to a measure of total income, of capital formation and consumption, the requisite total income must be a fundamental calculation. All the other subsequent tasks of planning will centre predominantly round the investment and production activity in the economy (with the monies so released providing the predominantly new purchasing power) rather than around 'priming the pump', with investment and production built up as a result. As such, policy for full employment in less advanced countries makes planning much more comprehensive in action and much more 'scientific' and technical. It may be noted that even in the U. S. A. policies of 'leaf raking', as they are called, have been considered inappropriate and inadequate, and a policy of disbursement on productive ventures has been called for.

### Its Gradations

At this stage, it is necessary to clear a deep-seated mistaken notion. The fundamental necessity for planning in full employment policy has often suffered a set-back on account of several assertions that there is no half way house between private enterprise and authoritarian politico-economic dictatorship; that planning either cannot exist in a 'free' economy or, if it does, the economy is really autocratic.<sup>1</sup> There is hardly any justification, however,

---

1. c.f. W. A. Lewis' answer, "the dispute about planning cuts right across left and right, and has nothing to do with the dispute about socialism". Principles of Economic Planning, page 8.



for this proposition that planning means leading 90% of one's life under permits and controls. That type of planning can certainly exist. The point though, is that even the comprehensive planning for agricultural countries we referred to, far from depicts that state of affairs. The hall-mark of planning is not interference with the private person's movements in economic life, but the complete knowledge of the structure and economic magnitudes existing and needed in the economy. Precisely what action is called for on the basis of that knowledge is a matter for choice from quite a considerable gradation of possibilities. It may be mere interest manipulation, or employment devices, or actual investment, or even complete control of investment and consumption—only the last of which would involve abrogation of much of the freedom of choice to the individual consumer in his daily economic life. Rationing or controls would also be no argument against planning. Rationing, whether in the production or consumption range of goods, is a concomitant of shortages and not of planning; and control, in the sphere of consumption goods, is not necessarily an adjunct of good planning, while in the sphere of investment and investment materials, it means really ensuring that wise direction which is sorely lacking in agricultural countries. State interference is also necessary not merely to direct but to initiate development, and to that extent planning would embrace these functions. It will hardly be disputed that efforts to rectify the existing economic situation are necessary. So long as policies adapted to that end do not interfere with freedom of consumption, there can be hardly any sensible ground for objection to adoption of the best devices. If planning is the method indicated, it is clearly above suspicion if properly interpreted. The planning we considered necessary for less advanced countries was predominantly from the investment and development angle and involved large scale interference in economic activity. But planning for investment and development does by no means imply 'planning' of consumption goods in the sense that traditional consumers' choice is abolished. On the other hand, planning first reckons the consumers' needs and directs production activity in a way capable of meeting just those needs.



It is chiefly for that reason that a plan is considered 'flexible'<sup>1</sup> (unlike a 'programme'). An indication that output under a plan does not in some respects meet consumption needs is meant to be, and is, reflected in a subsequent modification of the plan.

### Consumers' Choice

A word must be said about the nature of consumers' choice. In the economics of real life, all the normal variables and smooth continuities in curves which form the basis of 'consumers' sovereignty doctrines are, for several good reasons, not of real life. If so, our ceasing to act as if they were real would not bring much difference to anyone's way of life. An able statement of the whole point by Dobb is worth repetition. "In the first place, the problem of static adjustment to a given pattern of demand is matched in importance, if it is not dwarfed by dynamic problems concerning the development of the economy as a whole, development which is likely to change many of the variables in problems of static adjustment in ways which can only imperfectly be foreseen and allowed for until the changes occur.

Secondly, the static problem of allocating resources between different lines of production will be itself confined within the framework of certain strategic decisions concerning such things as the rate of investment (and hence the relative size of the capital goods industry and the form which new construction shall take), the location of industry, the relation between industry and agriculture, which of common admission constitute policy questions that cannot be satisfactorily decided by any verdict of a market. Thirdly, even within these limits, it seems probable that actual discontinuities on the side both of production and demand cause decisions about the proportions in which different consumer goods shall be produced to have a much narrower range of practicable alternatives between which to choose than economists who tend to think in terms of smooth curves of continuous variation have normally supposed. With regard to new commodities and varieties of a commodity catering for new wants, in no economic system can the market

---

1. Planning in Russia, for the sake of its very success, is prepared in three variants—according as the assumptions are normal, below normal and above normal.



afford any automatic index to guide production. Here the initiative must necessarily rest with the producer; an initiative which will inevitably play an educative role in the development of individual tastes and conventional standards. The power of choice between standardisation combined with cheapness and dearer variety will generally be conditioned straitly by the level of economic development that has at any time been reached (since this will determine how much variety the economy can afford—how far existing resources will stretch); and as we have earlier said, the essence of rising standards of living, as fruit of economic progress, probably consists quite as much in multiplying variety (and hence developing “new wants”) as in augmenting the quantity of familiar commodities which are already woven into the pattern of pre-existent consumer’s demand. At comparatively early stages of economic development the problem of allocation of labour between different consumer goods will be fairly simple. The resources available will not permit the number of alternatives to be large (if the maximum production of labour is to be achieved by making the fullest use of the advantage of specialisation and standardisation) and in the satisfaction of primary needs for food, clothing, house room and recreation, there is no very complex problem of individual consumer’s choice. At more advanced stages of economic development, the range of alternatives is much wider, and commodities concerning which consumer’s tasks are more varied and more fickle occupy a more prominent place. At the same time, when this more advanced stage has been reached, the equipment of industry and the production of labour will have grown sufficiently for the need to husband resources with studied economy to become much less urgent, and even to become a secondary matter: more latitude can be given to varying tastes by allowing a generous margin in the varieties placed before consumers, and a failure to allocate resources in precisely ‘optimum’ proportions will cost the community much less than when production was smaller and primary needs were still unsatisfied.”<sup>1</sup>

The point about planning is that it seeks to ensure the continuous satisfaction of an increasing range of consumption needs, realising

1. Soviet Economic Development, Pages 377-8. c.f. also Lewis’ Principles of Economic Planning, page 81. “At this stage of their development Russia and Eastern European countries...have fewer mistakes to make, and their planning, however rigid, cannot do as much damage as would rigid planning in (England)”;



as it does before-hand that under a system of development through unplanned 'individual commitments', and in the precarious context of a backward economy, consumers' needs are best only temporarily met; with the ultimate prospect being rather one of economic breakdown through both inadequacy and mis-direction of investment.<sup>1</sup>

### Modus Operandi

For planning in agricultural countries, knowledge about various economic magnitudes and requisites and actual responsibility for investment and production are, therefore, two basic and implicit factors.

The inability to use the demand side instead of investment in planning for full employment is due to the fact that a mere filling up of total demand to the brim means practically nothing in our context. Total demand consists of various ramifications. Corresponding to these lines of demand, the existence of lines of production is assumed; it is also assumed that those lines of production are amenable to demand incentive towards greater production. In our context, not only is the latter wanting but even some of the former are absent. In short, economic development—the only long term basis for full employment—cannot be expected to take place by mere provision of some economic 'climate' and of total demand. The latter type of planning really assumes that, between the two constituents of marginal efficiency of capital and propensity to consume, the former could be taken for granted and it is the latter that is deficient. In the backward economy this is hardly the case. The former is a far more serious deficiency.

It may also be necessary to mention that the desired type of planning does not eliminate the normal market processes for determining price in general. As such the question of price fixing by a Central Mind does not arise.<sup>2</sup>

1. c.f. American Economic Review, December, 1948, Page 814 Klein. One of the less known but most arresting cases of Planning in the Western world has been that of Norway since 1947. The licensing system there has been found to represent a workable co-operation between private enterprise and the Government, leading to a highly satisfactory allocation of scarce resources. "The most refreshing aspect...has been the attitude of the guiding economic theoreticians to disregard all pre-conceived notions about the supposedly optimal properties of a free market economy and to look for direct or indirect controls that will lead to an even higher level of economic welfare. They have done this work entirely in the democratic spirit so that one cannot find the slightest trace of the suppression of any fundamental human right in present-day Norway."

2. cf. Trotsky 'Soviet Economy in Danger,' page 33 quoted in A. P. Lerner. The Economics of Control, page 64 "Economic Accounting is unthinkable without market relations."



But this concession to market processes cannot imply that they could operate in any renegade laissez-faire setting. They have a role only in such a framework as appropriate redistributive taxation and subsidies, import and allied controls, and so on will allow.

The technique of planning is still in its infancy and its terminology is not yet crystallised. That does not imply, however, that its *modus operandi* is vague.<sup>1</sup> The first point to remember is that planning means, for economic activity, the best imaginable Co-ordination<sup>2</sup>—in concept and by definition it represents the highest and most comprehensive level. It is clear, therefore, that the essential and dominating nature of a Plan would be its inclusiveness, in the best possible pattern, of all modes of economic activity, every-one of which will be inter-related to every other. There would then be no place for independent policy-making units, like Tariff Boards and so on, which, although existing as entities, will live under the auspices of the Planning Authority. The purpose is to enable every problem to be viewed and decided in relation to the entire economy and its resources, real and financial, and not to any section of it. The same applies, therefore, to bodies like the Agricultural Advisory Boards, Fisheries Boards, Housing Committees and Advisory Committees for finance and exchange.

The first task of the Authority<sup>3</sup> would be to estimate (a) the total national income and (b) the desired total for the purposes of effective full employment. This latter total will then have to be modified, if so required by any limitation of natural resources. Such a presumption really assumes over-population in a strongly Malthusian sense. On the other hand, several different modifications will be called for. At this stage, the interest will shift from grand totals,

---

1. American Economic Review, December, 1948, Pages 798, 800, Klein—For instance, considerable elaboration is displayed in Norway's National Budget. It is divided into sub-budgets (1) manpower budget, (2) materials budget, (3) budget for the exchange of goods and services with foreign countries, (4) foreign exchange budget, (5) production budget, (6) consumption budget, (7) investment budget, (8) budget for the public sector, (9) the general budget. The goals are put forward as an investment policy, an employment policy, an export-import policy and a policy for each sector of the economy. In the fulfilment it was found that 'the only real errors' were in imports and to a lesser degree in exports. (This, it is said, shows up the difficulties of planning in an unplanned world).

2. c.f. Bukharin quoted by Dobb, Pages 203-4 where the concepts of "correct co-ordination of the various spheres of production" and "dynamic economic equilibrium" are clearly equated.

3. Gosplan had on its personnel "chiefly economists and engineers."



to magnitudes in various sectors of the economy. Now while the total productive capacity of the resources may well be enough to equate with total demand (or Income), the categories of goods which go to make the total in output are not likely to be exactly what the various demand streams in a Plan suggest.

Further, if the categories are exactly the same, still the productive capacity in the categories may differ from the demand amounts in each—one being more and another being less, than the corresponding demand. These are, incidentally, the rationale in international exchange of goods. The Planning Authority will allocate for export suitable amounts from those categories for which demand, in part or in whole, is not present within, but which are produced at less comparative cost and which can be expected to satisfy certain demand streams in other countries (for example, Tea, Rubber and Coconut). Those categories for which there is no corresponding demand stream anywhere in the world will have to be dropped out. From among those categories which can be produced at economic cost such items as are essential to the Plan will be retained. An important problem will be that of inadequate demand stream for certain categories within the country (and without), not because those categories are not consumed, but for reasons connected with comparative cost of production and sale. These cannot be met from imports, unless the possible total output exceeds total demand by such a margin as to eliminate the need for any such categories, through the remaining categories being exportable or capable internally of meeting requisite demand categories with satisfaction.

So long as all possible export categories have been fully explored, some of those streams which would normally be satisfied through cheaper commodities from outside, but which could, at some cost though, be met by internal resources should, by State intervention, be so met in an effort to prevent the level of imports from exceeding the ultimate export capacity. Which of these high cost categories should be contained within and which continued to be satisfied from outside has also been answered in our discussion of the international division of labour based on human skill and of the necessary basic industries (as defined by us) in an agricultural economy.<sup>1</sup>

1. It may be mentioned that any high-cost industries to replace imports are adopted only in the full satisfaction that imports cannot be paid for by new competitive exports. Much of the fairness of our point of view in Chapter 13 on the Havana Charter for example depends on such an outlook and attitude.



Any categories in the Plan for which no resources exist will (assuming export income is being put to optimum benefit) have to fall out. The remaining production possibilities in the country will be allowed only to the extent that financial resources permit and due regard is had to the priorities for development. The final Plan will be modified, quantitatively and qualitatively, by the foregoing influences.

At this point, to the extent that foreign borrowing is required, the principle of adjusting the level of imports to export capacity could be relaxed. But it could be relaxed only to a certain strictly definable limit.<sup>1</sup> The justification for the present adverse balance on this account is and must be such future exports surpluses as will repay these capital imports, plus what is represented as interest (and possibly profits) thereon. A decision on foreign borrowing clearly requires the best possible knowledge on future export capacity. To the extent that the expected future surpluses do not warrant an original figure set down for foreign borrowing, the problem has to be resolved by sufficient austerity or tightening up of belts in respect of present items of imports and the use of such margins for the necessary import of capital goods or whatever is considered necessary from outside to supplement internal resources. In this respect, the development programme will largely involve creation of import substitution industries.

The present exports themselves may form a substantial measure of the future surplus capacity when the development programme is through and the present categories of imports are much reduced and capital goods become a smaller flow than in the period of the Plan proper. In rough terms, if one calculates total export value plus any future exports and subtracts imports that must still be got from outside despite any development within, the remainder will represent the annual repayments on loan and interest account. This result should be able to decide how much could be borrowed from outside.

---

1. "Large grain exports (from Russia) are not due to an existing surplus but due to the fact that in the estimation of Moscow the needs of the Soviet consumer come a long way behind the requirements of economic planning..." *Economist*, March 4th, 1950, Page 488. Analogous is also the availability of several British goods overseas but not at home.



In any case the need for internal saving is paramount, and, as we saw, the amount needed is considerable. A dependence on internal savings alone may or may not be possible;<sup>1</sup> the chances are it will not. Once the two quantities, of possible foreign borrowing and internal savings, are known the rate at which development can proceed becomes determined. For the calculation is a straightforward one of relating the total value of investment required under the Plan (i.e. value estimated to be necessary to create the total production stream envisaged) to the total value of savings available every year. At this stage we enter the field of more conventional terminology and we could talk of a four-year plan or fifteen-year plan<sup>2</sup> and so on.

Once these adjustments are clarified, the next stage will be to initiate production itself<sup>3</sup> along the lines planned out. At this stage there are some further adjustments required both to make the plan realistic and to give shape to the programmes within. The programmes are to the Plan as action is to the Idea.

Not all the calculations based on Incomes, Resources and Savings will work without full reckoning of all limitations and considerations in the practical implementation of the Plan. The timing of public investment, for instance, is as crucial as the factors so far considered. If, for example, the capacity of the Plan to be translated into action is, from a technical point of view, less than

1. Note also the point that "corporate taxes in a developed economy are of less importance than personal taxes." In the U. S. A. e.g. in 1941, direct taxes on corporation are estimated to be \$11.5 billion against \$19 billion by individuals. In the U. K. it is roughly half and half. *Eastern Economist*, March 3rd, 1950, Pages 339-40.

2. c.f. Dobb quoting Strumilin on Russian Planning, Page 326. "Capital investments of previous years and the previous harvest determine in advance almost 100% of the economy of the coming year in the field of production, imports and exports, the budget, credit, etc. The possibility of a new arrangement of the existing production powers so as to attain a more effective combination of them is very limited indeed within one year. They are already much bigger for a period of five years; for a period of ten or fifteen years, with a high rate of accumulation, they are even enormous. And if each plan constitutes a blend of elements of forecast as to what is objectively unavoidable with planning of what is desirable, forecast takes first place in annual plans and planned direction in the several-year plans."

3. In fact "the process of putting a plan into operation is itself part of the process of fitting it to actual data and of testing out its correspondence with reality. Such a process cannot be confined to the stage when the Plan is being put on paper for the first time."

Dobb, on Russian Planning, Page 337.



that warranted by other resources, then certainly an overlooking of this is only bound to result in some mis-firing. This could only create bottlenecks and will, probably, result in spilling over of unproductive purchasing power into the economy, thus only straining further the balance of payments or the inflationary situation. It produces consequences similar to expenditure in the absence of a Plan. For instance, a large investment (say, a huge Tank) requires the automatic co-ordination of all other activities of forest clearing, manuring, sowing, marketing, etc., and above all a permanent population; but such investment though so eminently sound under a Plan ready for practical execution, becomes, by itself, so much additional strain on the limited recuperative forces in the economy. If the lack of co-ordination is sufficiently delayed to depreciate overwhelmingly the assets created by a single investment that work becomes also abortive.<sup>1</sup>

The timing of investment and all that it means has been given growing importance in full employment policy for advanced countries themselves. It is of more importance in agricultural countries.<sup>2</sup> The financial aspects of timing are not, of course, exactly the same in agricultural countries. The problem is not so much one of counter cyclical timing, but of deciding the maximum quantities of financial resources that can be commanded for implementing the plan.

1. c.f. *Economist*, May 10, 1952, page 355, Colombo Plan's First Years. "In some cases there has been quite unwarranted procrastination; technicians have been asked for and then kept kicking their heels; capital equipment has been ordered for schemes before buildings were provided to house it; and expensive machinery has been left in the open to rust and disintegrate." There is need for a "realistic appraisal of priorities" in this sense too.

2. There was e.g. some doubt about proceeding according to schedule with the Damodar Valley Project in West Bengal. During such doubts on timing and phasing, considerations like the following, if already existing, would be most helpful. "It will provide the Government of West Bengal, on completion, a net revenue estimated at Rs. 123 lakhs....The gross revenue to the Government of West Bengal is of the order of Rs. 2.6 crores; and the addition to the national economy from crops alone in West Bengal and Bihar is Rs. 15 crores if rice sells only for Rs. 15 per maund and about Rs. 5 crores from power, apart from other income from undertakings which this power will serve. The scheme will in addition provide considerable new employment....On the assumption that the total income attributable to Damodar (not just to the Corporation) after completion is Rs. 21 crores the return to the country is of the order of 30%. This is a very conservative estimate....Damodar has the exceptional advantage that some of this revenue will....flow in about 18 months and the revenue from the power after (final completion) will be immediate because undertakings are already there to provide nearly full demand.... In the case of Damodar for which \$30 million are likely to be received from the World Bank and the Government of India together, only a sum of about \$18 million in addition seems essential....The loss (through a longer phasing of the project from 5 to 10 years) is Rs. 13.13



As production gets under way, of course, more and more attention has to be paid to the question of leaving the population with sufficient purchasing power to consume the new output. The technical problems relating to public investment have much in common with the West; in relation to some aspects like engineering they are far more difficult. There are also the legal and administrative problems which have been succinctly expressed in the following passage: "Before funds can be spent on public investment, agencies must exist with authority and organisation to spend them. In most countries agencies will be required both at the central and at the local levels of government. The development of such agencies into smooth-working machines takes considerable time, and unless they are in existence when the need for expansion arises, and have full legal authority to do this job, serious delays may result. Legal authority can be conferred as a rule only by legislation. In addition, a series of important questions have to be considered, such as the desirability of appropriating funds in advance if delays are to be avoided, and the advance letting of contracts.

"The acquisition of sites might be one of the most time-consuming of the legal operations that must precede the institution of public works projects. Open market purchase of land involves lengthy negotiations. An alternative procedure is to obtain land by condemnation procedures. Most countries have expropriation powers, but they are often limited in scope and slow in their operation."<sup>1</sup> On the engineering aspect, a discussion for advanced countries states that it is not necessary to give much weight to it in assigning priorities to projects. It is not an exaggeration to say that in agricultural countries just the opposite could be the truth. It should of course be the endeavour of the planning authority to lay down priorities from the point of view of economic need, but the question of training and skill of labour and executive will, if neglected, certainly

---

crores to the Corporation in addition to the postponement of the realisation of the peak national income of Rs. 21 crores per annum to the country which reckoned over all may be at about Rs. 80 crores." *Eastern Economist*, November 11th, 1949, Page 737-8

1. I. L. O. "Public Investment and Full Employment"—Page 297.



upset the priorities in the plan itself. "The engineering aspects of timing have two phases; time from contract award to beginning of construction (engineering and planning phase); and time from beginning to end of construction, (construction phase)."<sup>1</sup> The engineering planning phase together with costing is important to the drawing up of the plan itself, and the construction phase to the execution of that Plan.

All these factors are very likely to influence the period required for execution of the Plan. At the same time it may be said that it is precisely these difficulties that call for complete co-ordination and planning. There is also another factor which is important not only for the period of the Plan but also the priorities in it. We have referred to the location of industries as a factor to be reckoned with; we have seen, however, the need for mobility of labour for securing of optimum results. The settling of the claims of resources and labour (if they conflict) in deciding location and the decisions on mobility required must be reckoned well ahead if the period of the Plan is to represent some truth and if the priorities in the programmes are not to be upset later.

It is the non-recognition of these problems that could have led to such statements as the following: "Our difficulties in the way of spending monies on public works is seen by considering the programme of work of the Public Works Department. Inclusive of supplementary estimates, Rs. 33,000,000 was provided for expenditure in 1948-49. Up to the end of September, 1949, estimated actual expenditure will be only Rs. 17,000,000. The main reasons for these differences are (a) Inclusion of provision for expenditure before Sites have been settled, (b) Lack of technical and supervisory staff, (c) Shortage of materials." There is also this passage which is illuminating: "No doubt Government has increased its expenditure which was Rs. 250,000,000 in 1944 to Rs. 666,000,000 in 1948, and though the total monies expended in Ceylon has increased from Rs. 685,000,000 in 1944 to Rs. 719,000,000 in 1948, it would seem that this increase has not created full employment, because the direction on spending has not been properly chosen or

---

1. *ibid*, Page 297.



that there are some causes which we are unaware of which keep away employment although money was spent on a larger scale in 1948 than 1944.”<sup>1</sup>

If we have reckoned with these we could with more definiteness talk of the length of the plan and say with some certainty that it would take five years or ten years, or fifteen years as the case may be. But we should still not have the full body of the Plan. A phasing out into periods is required. This phasing is possible only now, because, although we have talked of priorities, we would only at this stage be able to draw this up with completeness. Of course, the conditions determining priorities are not the same as in advanced countries; the fundamental requirements of development have already laid down a scheme wherein production of wage-goods occupy a high place in the list. Whatever limitations the other factors, like location and engineering, may impose, must as far as possible be subordinate to this more fundamental argument. Therefore, even at the expense of a longer Plan one must sacrifice ‘leaf-raking’ as a high priority item even though it surmounts most problems of location and engineering.

There is also another type of limitation which needs to be realised very clearly. The first stage of the Plan is expected while serving the Scheme of Development to give early resilience to the economy; so that, at a second stage, continued investment or heavy capital consuming investment will not topple the balance of payments badly. We cannot dump all the moneys on Agricultural Colonies exclusively (even Factories exclusively). There is a great difference between one or two Gal Oya Schemes at a time and ten. A maintenance of balanced development, as between agriculture and industry in both economic and ‘technical’ senses (e.g. Bottles in relation to fruit canning) and so on, is imperative. Within this balance too, further care is required. If, for instance, the first phase is 5 years, a ‘Gal Oya’ scheme may not produce anything like its expected output within 5 years. As such, smaller, and quicker methods must go side by side.

---

1. Budget Speech (Ceylon) 1949-50, c.f. Eastern Economist, June 18th, 1948, Page 1090—“A second round of inflation has been created very largely by unco-ordinated Governmental outlay on schemes of every kind financed mainly by currency expansion and the depletion of old funds. Capital outlay should therefore be immediately restricted and there should obviously be concentration only on such schemes as would add materially to the production of consumption goods.”



These considerations should also help clarify that one cannot plan according to, and within the framework only of, investment resources available for the time being and from time to time. This is so especially if it means framing a 'total' or over-all Plan within the limit of such resources. A Master Plan in terms of total required resources is essential. Investment resources, not always only those at the moment available, can reasonably be utilised only in terms of such a Plan.

Planning may be assigned four main aspects: preparation of the Master Plan (namely a concrete expression of decisions made by the planning authority as to the desired physical form and public personnel of the community), preparation of specifications and working drawings, financial planning, and programming. The essential problem of the programming is the assignment of priorities for various projects.<sup>1</sup> There is some difficulty, if a full employment programme will take fifteen years, in knowing whether the term Plan is applicable only to the entire period and whether anything inside it is part of the programmes going to make up the plan. In terms of the foregoing description of Planning aspects it would not be inappropriate to talk of a five year Plan—so long as the planning authority gives the concrete expression referred to as to the desired physical form and public personnel of the community, not only in respect of fifteen years hence (when there will be full employment) but also in respect of five or ten years hence and treats each of these landmarks as targets, representing a certain attainment in employment and income. It is clear however, that all projects within any Plan are part of the programmes; and by no means Plans. The programme will indicate the various projects to be taken up year by year over the entire period of the Plan. It will therefore be evident that to talk of a Programme as such is nonsense if there is no underlying Plan. It would be blind even as a plan would be empty, if it were not followed up by effective programmes. That would seem to be the weakness with most Plans.

Although by a roundabout method we should have ascertained earlier the total cost of the Plan, it is now that a realistic calculation

---

1. Incidentally, c.f. Dobb, Page 19, "The smaller the variety in production the more obvious and the less controversial is likely to be the decision about what are the essential priorities."



would be possible. For with full awareness of all the projects and their costs as determined finally by both financial and technical needs, the total money burden under the Plan becomes measured up in the best possible manner. The result of this calculation and the earlier figure should more or less tally, since they both refer to the same target. In the earlier case, it is by taking some average capital investment per head or per unit of income; here it is by actual assessment of capital needs in each case. Further, with the priorities now determined, a clear statement emerges as to how much finance is involved every year under the Plan, and how much exactly on every project. With co-ordination already implicit, there should be no fear of disturbing disbursements in a year because there is under the Plan complementarity (both physically and chronologically) in development. The ordering of engineering skill and of finance will correspond to the pattern laid down in the priorities for projects; no resources will be wasted on superfluous training, nor any unnecessary finance raised as can well wait. The need for planning arose from the great need for the most economical utilisation of the conspicuously limited effective resources of agricultural countries; the indisputable need for co-ordination of every type of economic activity is its hall-mark. Failure to co-ordinate can result in anything ranging from a larger call on the country's financial resources, to a worse economic plight than the present—of which the manifestations may be enormous foreign commitments, continued adverse balances (alternatively inflationary pressure within), unemployment and under-employment probably worse than before the programme of 'development.' A planner has been defined as "a specialist in seeing the relations between and co-relating the work of specialists."<sup>1</sup> It is an admirable definition and that should effectively convey both his role and the need for his role.

Planning is not merely a central affair; it has to exist at several levels.<sup>2</sup> It will be evident that assessing financial costs of required output of the various categories of production was based on a

---

1. Krishna—'Digest of Plans' Page 96.

2. Gosplan had its sub-organs geographically, in every republic, region and rayon or local district; and through the economic administration, in the Commissariat, the trust and the factory (Dobb, Pages 322 and 333). It may be interesting to note that local industry serving primarily the local market, and drawing its own material from local sources in the main, is administered by the local bodies, whether it be region, province or municipality.—Dobb, Page 343.



complete scientific, statistical, technical, and financial appraisal of every one of the individual projects. It is natural that these should all function under separate 'Plans' for themselves too. These Plans would of course be within the framework of the Larger Plan, and the priorities and the finances allotted by the latter to each project will determine the period and the magnitude for which each of these projects will themselves plan. For instance, the Cotton and the Clothing categories will probably plan for large scale development and within the first few years itself, while Glass will be small in scale, say, to provide bottles to export fruits in syrup, and may be not given a place till the second year or so; similarly a Fertilizer Plant may get much more importance and a Steel Rolling Plant much less; and each of these units will then plan to fit into the Central Plan. Without the Central Plan, 'free' forces may create large glass factories when it is not the need of the hour, or may create only cotton farms and leave all else undone and development sacrificed. So long as the necessity for the smaller Plans to function within the framework of the Larger Plan is recognised, the former planning must be both comprehensive and advanced. Several of the details like needs, supply, investment costs, and so on, would already have been assessed in the framing of the Central Plan. But the Central Plan itself would have modified these where necessary in respect of time, skill and the like. The individual units will now plan in this subordinate context.

Suppose we take Salt as a case. There will be for the industry a separate Planning Committee which will assess the present supply and consumption; and the needs of the country (need being now identified with the target under the Central Plan) for (a) Human Consumption, (b) Cattle and Agriculture, (c) Chemical Industries, (d) Export (in case of an Export Programme under the Plan). It may be that one or more of these is left over for the second five year period of the Plan in view of the urgent needs elsewhere for financial resources or some like reason; if so, the Plan for this industry would be affected correspondingly. On the supply side, questions such as (a) Total area under Salt Production, (b) Total average production during the last five or ten years, (c) Percentage of Salt production per acre, (d) Measuring of average production in terms of methods, mechanisation, industrial peace, area, economical grouping, and fixing of targets, are involved.



It is clear that all these tasks will call for much technical and scientific knowledge and ability. Every field of economic activity must have its expert committees. It is these committees that will provide, as planning boards, the necessary information about demand, supply, technique and costs to the Central Planning Body in the latter's tasks of drawing up the Central Plan.<sup>1</sup> To take one interesting instance, there is the case of the Palmgur Industry, the manufacture of sugar from the Palmyra Palm juice. There is first the question of adequacy of this source for the entire supply, and therefore the question of supplementing from cane sugar.<sup>2</sup> There is then before the implementation, the question of technique and costs of production. It would appear that cane plantations lend themselves much easier to the economies of large scale production in almost every aspect.

On a calculation of how much sugar could be strained from palm juice one may very probably find that the extent of collection required and the costs incurred will be excessive. Nor is quick planting possible and lapse in regular replanting will show itself suddenly as a gap about fifteen to twenty years hence when the economy is least ready for it. On the other hand, it may be possible to establish central collection depots, to which any one tendering supplies of juice could bring the stuff. This may make collection

---

1. All direct action by the State in economic development (i.e. in actual implementation and administration) should not be by Heads of Departments but on the T. V. A. model (i.e. entrepreneurial or managerial system). Incidentally, c.f. Bauer "The experience of rubber regulation (the reference was not to Ceylon) also emphasises that when Government interferes in economic affairs, the lack of knowledge of economics on the part of civil servants is likely to prove a serious drawback." As for the Planning Body itself, Russian experience saw a similar weakness in the setting of differences between the Body and the Government departments by unprincipled mutual compromises and attitudes 'too uncritical towards departmental projects.'—Dobb, Page 318.

2. In actual fact it provides an interesting case for exploitation in India. The facts are as follows: "There are about 50 million palm trees in India, of which about 40 million are palmyra, and the rest are date palms. It has been estimated that a proper exploitation of these trees can create employment for more than 5 million families, besides producing large quantities of gur and gur-products. The conversion cost of palm juice into gur is very low and the manufacturing process is also extremely simple. Only a few tools and accessories are required in the conversion process, thereby enabling a family to earn its living with a very moderate investment. Twenty palm trees could suffice to produce about 2,000 lbs of gur a year valued at Rs. 500. The total expenses involved in the manufacture of gur do not exceed Rs. 50 giving a net income of Rs. 450 to a family. Similarly, a family of one man and one woman could produce about 3,000 lbs of gur from date palms and earn about Rs. 650 as their wages." Eastern Economist, May 6th, 1949, Page 735.



economical. All in all however, cane sugar may be yet cheaper for the country. These calculations it will be noted, call for all the technical and costing abilities that the subordinate Committees referred to must needs have. It would appear at first sight that the Central Planning Committee could then straight decide for cane and against Palmgur. That would not, however, be necessarily the case. The individual calculations submitted by the Committees do not comprehend the overall picture envisaged under the Central Plan for the economy. The area covered by the palm may already have been located (on considerations such as we saw in the previous chapters) as requiring Cottage industries, the alternative being under-employment. In which case the Palmgur Industry may have in any case to be established. That would, of course presume that such area and population as would otherwise have taken to sugar, will be put to optimum use in other productive sectors of economic activity.

Alternatively, it may be that there are other subsidiary occupations (which are not high cost) in the palm area such as mixed farming itself or, if that is not possible further, other handicrafts. In general, where costing results cast some doubt on economic feasibility, it will be found that if rural produce depends on individuality and artistic variety they would find the ideal output for the population surplus.

This is only an indication of the nature of the problems involved. As we said specialists will be operating in every field. Suffice it to say that seeing the relations between, and co-relating their work, will be the task of the Central Planning Body.

### **A Theoretical Model**

A theoretical study made recently for South East Europe in terms of models is interesting. Though it neglects all development in agriculture, it provides much insight into the economics of its postulated full employment programme. Some of the more significant facts relating to development in South East Europe may be therefore noted. Of a total population of 42 million the active surplus population is 6 million; and for every 750 absorbed in industry about 250 is absorbed in the services. The direction of



development is not conspicuously different from that envisaged in our previous pages. It is interesting to see that one of the first points raised is the vast extent of 'socially useful work' really available, but which must still be modified if development is to take place. "In a period of rapid industrialisation it is hardly possible to satisfy in full all the Building requirements, including complete rehousing of the new industrial population. We must therefore cut down the programme to what is essential for preserving productive efficiency, and preventing undue hardship."<sup>1</sup> The standard figures of capital, power, materials and output per occupied person are next set down. (vide page 236 below).

The point is then clearly brought out that there can be a discrepancy between output and demand and that the former must really be planned for the latter. The following chart on Page 237 is illuminating.

This adjustment is finalised with reference to comparative cost and related factors. To this end industries are classified as follows:<sup>2</sup> Light Industries—building, clothing, furniture, textiles, leather, light metals; Medium Industries—building materials, semi-manufactured metal, paper and printing, metal extraction and refining; Heavy Industries—food, etc., mining, chemicals, electricity (and water power). Preference has been given to light industries in this final adjustment, but with important qualifications.<sup>3</sup>

For example "where transport forms a significant cost item either because the industries concerned consume large amounts of raw materials per unit of output, or because the final product is heavy relative to its value, nearness to the source of materials or to markets is important. In our case the food and chemical industries (or certain sections of them) have obvious advantages on this account, and we have therefore expanded them although they are on the average heavy if run on modern lines". As regards any possible

- 
1. Mandelbaum, Page 30.
  2. Page 62.
  3. Page 63.



## STANDARD FIGURES OF CAPITAL, POWER, MATERIALS AND OUTPUT PER OCCUPIED PERSON

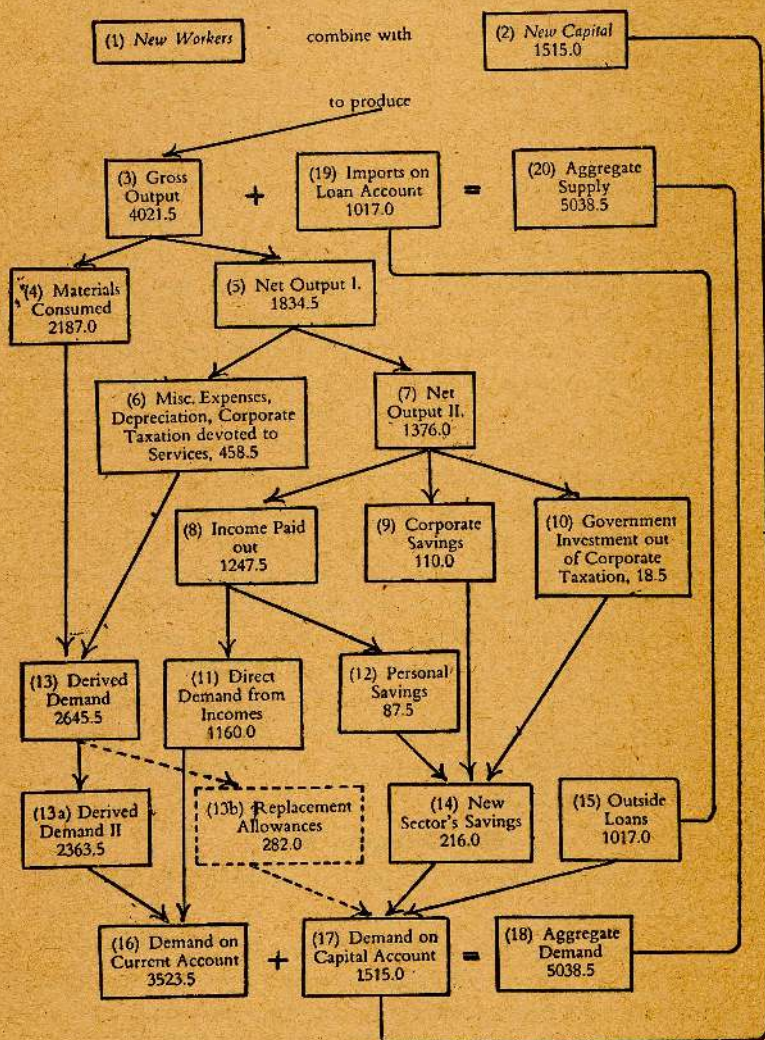
Industry	Total	CAPITAL (£)			H.P. Power Installed	Materials Total	ANNUAL FLOW (£)		Gross Output
		Land & Buildings	Plant & Machinery	Working Capital			Consumed	Net Output	
	2	3	4	5	6	7	8	9	10
A. Mining & Electricity									
1. Mining ...	830	300	400	130	4.0	60	18	200	260
2. Electricity ...	6000	1900	3800	300	200.0	250	180	950	1200
B. Building	120	60	50	60	0.2	150	5	150	300
C. Manufacturing ...									
1. Food, Drink, Tobacco	650	200	250	200	3.5	800	25	300	1100
2. Clothing & Bedding	200	90	30	80	0.5	180	5	120	300
3. Textiles ...	300	90	120	90	2.0	300	15	150	450
4. Leather, Fur, Rubber	300	120	80	100	2.5	470	15	180	650
5. Chemicals ...	1000	220	550	230	4.0	630	40	370	1000
6. Paper, Stationery, Printing	450	160	200	90	3.5	220	20	280	500
7. Furniture, Woodwork & Pottery & Glass Misc.	200	100	60	40	1.5	200	15	150	350
8. Building Materials	350	120	150	80	4.0	230	25	170	400
9. Light Metal & Electricity Products	300	100	100	100	2.0	240	15	180	420
10. Semi-manufactured metals engineering ...	350	140	120	90	2.5	180	15	170	350
11. Metal extraction & refining	550	130	270	150	7.5	820	90	330	1150



*The Industrialisation of Backward Areas*

CIRCULAR FLOW, FIRST FIVE-YEAR PERIOD

(All figures in million £)





surpluses and deficits in production there is the following observation. "Any surpluses of production over demand should be in certain industries (notably in food and perhaps in chemicals) . . . the requirements in building and building materials should be covered and . . . any deficits should be concentrated in the remaining heavy industries, namely semi-manufactured metals and engineering."<sup>1</sup> We may, however, note what we have said about possible high cost of rice farming in Ceylon. If so, effective planning would need not merely to allocate targets but set limits as well. The net deficit in the assumed production programme for South-east Europe is estimated, in relation to demand, to be thousand million pounds for the five years, or two hundred million pounds per year.

"If we exclude the demand for land, somewhat less than half of the deficit consists of capital goods and the remainder of consumption goods, semi-finished products and especially raw materials. This deficit—the excess of aggregate demand over gross output—represents imports on loan account: Item 19 of our scheme of the circular flow. It is equivalent in that scheme to Item 15: outside loans from the old sector and/or from foreign countries."<sup>2</sup> Meeting effective demand would involve some such consequences. "Rich countries suffering from unemployment need not create new capacities if they want to provide additional work. In economically backward areas, however, increased (productive) employment is conditioned by an expansion in factory equipment and in such basic services as transport and housing. High capital outlay is therefore unavoidable particularly during the early stages of industrial progress."<sup>3</sup> Of course, measures like double or triple shifts in factories can reduce capital equipment required per worker and the economic burden involved in development.

The rate of saving is estimated at 6%, but it is admitted that 8% is far from impracticable.

### **The Colombo Plan**

A brief reference to the Colombo Plan would be apposite in this Chapter.

Two features may first be noted regarding the Colombo Plan.

(a) Its implementation is expected not so much to raise the standard of living of the countries concerned, as to prevent a deterioration in

---

1. Page 64.  
2. Page 76.  
3. Page 83.



it. The Report of the Consultative Committee on its Fourth Meeting, which is also the First Annual Report on the progress under the Plan, is clearly aware of this. "The implementation of the development programmes is essential to arrest the decline in the present low standard of living and to provide a foundation for further improvement."<sup>1</sup> (b) The second feature is that it is not a "centrally planned and directed blue print."<sup>1</sup> Investment planned refers to the public sector. Active planning is also confined to that sector, although the output and potentialities in the private sector are taken into account in determining the nature and degree of investment in the public sector. The Colombo Plan is not confined to providing basic utilities. It covers the economy comprehensively and seeks, by widening the scope, to make good the deficiencies in the economy. It thus covers a large range of the 'wage-goods' industries as defined by us. A random selection of items in the Plan for Ceylon shows the inclusion of paddy, cotton and sugar cane cultivation, expansion of forests, supply of power, fishing, and the manufacture of salt, cotton goods, sugar, fertiliser, cement, glass, tiles and brick, ply-wood and paper.

Apart from the arrangements for capital assistance, the outstanding feature in the implementation has been the Scheme for Technical Co-operation, whereby technical assistance is to be rendered by the countries to one another to a value of £8 million over a period of three years from 1st July, 1950. That this has been decided in addition to the existing Expanded Technical Assistance Programme of the United Nations and the specialised Agencies, and the United States 'Point Four' programme, is sufficient acknowledgement of the crucial importance of 'skill' that we referred to in previous pages.

The Colombo Plan, as it worked out so far, has also illustrated the need for maintaining 'flexibility' in planning. The premises on which a plan will have been worked out can always change. Several such changes marked the implementation of the Colombo Plan. For instance the terms of trade changed so favourably owing to the Korean war that the planned deficits in the balances of payments became surpluses. Development in 1950-1 (in some cases also for 1951-2) was financed entirely without borrowing. But the plan could not be altered to take full advantage of this. Immediate speeding up of development expenditure was not

---

1. Page 3.



possible. Additional capital goods were not available at short notice. There were shortages of experts as well as skilled and semi-skilled workers.<sup>1</sup>

On the other hand, the terms of trade changed adversely towards the end of 1951. Coupled with the sterling crisis from the middle of 1951, it provided a strong set-back to development programmes. The Colombo Plan countries had to depend largely on their own resources to the extent that dollar restrictions were introduced; account had also to be taken of the economic bottlenecks of the industrial countries of the Sterling Area.

The Plan for India was affected by another fortuitous factor for which suitable adjustment had to be made. It was the disastrous drought in 1951-52. It resulted in a 'large increase' in the balance of payments deficit.<sup>2</sup>

The future years for the Colombo Plan countries may witness a further deterioration in terms of trade and balance of payments and a depletion of sterling Assets and similar resources. Planning must then be capable of making the appropriate adjustments. It is evident that the Colombo Plan countries have seen the need to do so and that they do not regard their Plan as a rigid Blue Print.

The Plan for Ceylon was originally estimated at Rs. 1,359 million and meant to cover "only the major items of Ceylon's net capital investment." The revised estimate is Rs. 3,200 million and represents total gross capital investment by the Government. This figure is reckoned 'the minimum development necessary and practicable'.

The following table<sup>3</sup> giving the revised programme under the main heads may be set down for information and some comments.

	Cost in (million) Rs.	Percent of Total
Agriculture and Multi-purpose projects	900	28
Transport and Communications ...	600	19
Fuel and Power (including coal) ...	150	5
Industry ...	200	6
Social Capital ...	758	24
Rural Development ...	400	12
Research ...	25	1
Miscellaneous ...	167	5
	<u>3,200</u>	<u>100</u>

1. Page 18.    2. Page 33.    3. Extract from Table at Page 24.



The proportions in which the sums above are distributed among the heads is important. Investment in any sector constitutes, chiefly through wage bills, an increase in total consumption demand not immediately counter balanced by increased home production in consumption goods. It takes long to set up industrial plants for cement, fertilisers, paper and similar projects. It is longer in the case of River Valley Projects. Building of roads, by themselves, show little commensurate increase in consumption supply for a long time. The same may be said of most items under Social Capital. While the last are necessary for agricultural and industrial development, they will not, unaccompanied by such development, match the increased demand for consumption goods except in a limited form. Hence the need for co-ordinated development, as stressed in an earlier chapter.

Viewed in this light, the items Industry, Social Capital and Rural Development seem to call for some comment. The percentage of total expenditure allotted to industry seems small. This judgement refers only to the relative orders of magnitude. The official estimates are themselves called 'tentative' and an 'indication of relative orders of magnitude.'<sup>1</sup> This seems low when it is seen that multi-purpose projects, are described in the Report as 'mainly agricultural'. 'Rural Development is meant to solve under-employment among the 'immobile labour in the rural sector.' Expenditure on it constitutes a large percentage under the revised programme. It is said to be for 'construction of houses, roads, bridges, wells and irrigation channels.'<sup>2</sup> It pertains partly to agriculture, partly to transport and partly to Social Capital. Division of the 12% allocated to it into these 3 components raises the percentages for agriculture to about 32, Transport to 23 and Social Capital to 27. The last two then take up 50% of the entire expenditure under the programme. This may need further consideration as there are already multi-purpose projects involving nearly  $\frac{1}{2}$  the total expenditure on agriculture (Fisheries are included in the item Agriculture), whose 'gestation' period is quite long. Transport and Social Capital are important indeed. The question

---

1. Page 24.

2. Page 30.



is whether, the economy can stand the highly 'consumption-increasing' nature of these expenditures at the inauguration of a Plan. The Rural Development Movement itself, like the Community Development Projects in India, is a most happy idea from the point of view of harnessing the spirit, will and human interest so necessary to the implementing of a Plan. This human factor is necessary anywhere for genuine success, and is even more urgent in under-developed countries. But it will be highly important to the fructifying of the Plan to decide into what channels the constructive forces should be canalised.

The country has been so far lucky. The sudden boosting up of export prices, chiefly as a result of the Korean war, enabled (despite devaluation) both the investment in industry and multi-purpose projects and the expenditure on Transport and Social Capital. It is doubtful whether the same good fortune will continue. The terms of trade which stood at 123 in March 1951 and 100 in June of that year, had gone down to 89 in September and 83 by November.<sup>1</sup> If the boom conditions do not hold it is unwise to spend the sum mentioned in the programme on Rural Development as an item. For the pressure on 'consumption-imports' will be rendered well nigh excessive by expenditure on Transport and Social Capital alone. Rs. 400 million at this stage on Rural Development will only make the effects of that pressure more certain.

It should be wiser if the Plan concentrated now much more on Industry. The percentage of total expenditure on Industry would thus be greatly stepped up and made smaller in later Plans. The result would be that agricultural and industrial output for consumption purposes would have greatly increased at the end of the next five years, and would enable a concentration of expenditure in a later Plan on Social Capital without involving the economy in a Payments crisis.

The aim of the Rural Development project is stated to be the overcoming of under-employment in the rural sector. Its work roughly covers items pertaining to Agriculture, Transport and

---

1. Page 23.



Social Capital. Apparently, it does not touch cottage industry. We have seen in another chapter the vital role of cottage industry in industrial development. It is a better policy to intensify work on cottage industries. With increased skill in cottage crafts and industries, the contribution to the economy will be considerable. This will also meet the problem of immobile labour as well as under-employment. A small amount may be left to supplement (through the building of houses, roads, wells etc. by the under-employed) a cottage industry programme. (This should go a considerable way as Rural Development work should essentially be on a self-help basis). The rest may with profit be transferred to the item Industry. Cottage industry may even be the chief industrial feature, in the manner of the small-scale watch making units in Switzerland, or it may be the basis for the industrial structure of the economy, as it largely has been in Japan. In this connection, the allocation for Research in the Revised Programme is extremely wise. The sum may in fact be increased as the range necessarily covers Agriculture and industry as well, and cottage industry may get short shrift at the hands of these two. Research is essential to exploit the hidden potentialities in the innumerable cottage industry raw materials.

Since the aim of the Plan is to prevent the Country's standard of living from slipping down, it seems very necessary to consider the priorities in the Programme with great care.

### Some Implications of Planning

To return to our subject proper, certain points relating to financial policy and so on may be briefly mentioned.<sup>1</sup> Proper finance, sound wage and price policies, and efficient marketing are absolutely essential. Without the proper lubrication, robust and correct flow of blood, and actual finalising of the end of all activity, viz. consumption, half the purpose of planning and production is lost.

---

1. On the whole subject of planning and of the role of Finance as well as the questions of incentive, consumer's choice, etc., c.f. Dobb. With regard to the Financial Plan, it stands alongside the Production Plan and is constituted by a Credit Plan (credit from Banks to Industry), a Cash Plan (largely the Wages Bill) and the Budget (reflecting the role of the Turnover Tax which has already appeared in the Cash Plan) Dobb, Page 348.



### **The Budget**

In the first place, there is the new outlook on the budget and on budgeting. It is not possible in this thesis to detail all the relevant principles and concepts in regard to this aspect of planning. Suffice it to say that the Annual Budget ceases to be pre-eminent. With the removal of any sanctity in the idea of the 'balanced budget', the Annual budget will increasingly become part of and subject to the larger Development Budget which would cover the entire period of the Plan. Balancing of the budget will not be over a year, but in the context of a long period—extending even beyond the first in a series of six year plans. The setting of the Development Budget will be in terms of loan-finance to a large degree and the annual budget will reflect that increased importance in a new measure. The Annual Budget will also cease to be a mere add-up of departmental estimates and reflect and include the investment aspects of the development budget. Of course, this is not to say that the Annual Budget cannot be separated from the Development Budget; in fact capital expenditures must be more clearly separated than now from current expenditure. What is observed is that, in a given year, the financial proposals of a country under Planning will be different from what they are now. There are also other points, like the doubt as to whether certain works would then come under the Annual Budget or the Development Budget. The whole subject provides interesting and necessary study. But the fact that we are not engaged in a study on Planning alone, but on a field more comprehensive, prevents us from probing in any further detail.

### **Exchange Policy**

Secondly, a sound Exchange rate policy is fundamental. It is not necessarily sound to rely on exchange depreciation to rectify an adverse change in the balance of trade. Our export income cannot be increased by devaluation. The prices of imported consumption goods go up and can even partly be off set only by heavy burdens on the government's subsidies policy. The capital equipment will be imported at high cost. In a country depending (till the transition is over), on imported consumption goods, and embarking on economic development, there



is no place for the traditional implications of devaluations. Devaluation achieves its objects by making imports more expensive and exports more cheap. It aims at *reducing* import volumes and increasing exports by a greater proportion than the respective changes in their prices.

An interesting case study, mentioned by W.A. Lewis,<sup>1</sup> is worth noting even though the two countries referred to are industrial countries. He refers to Britain's post-war adverse balances, characterises the foreign demand for her exports as "very inelastic" and strongly opposes depreciation in the circumstances. Appreciation, he says, would have been better, and cites Belgium in evidence. According to calculations made by E.C.E., the Belgium index of commodities available for home use in the year June 1946—June 1947 (base year 1938) was 123, while the U.K.'s was only 95. On the other hand, Belgian production index was only 94, while Britain's was 108. The explanation is in the following data. Belgian import index was 120 and export 71 (first 9 months of 47); Britain's was 77 and 106 respectively. Belgium was selling at high prices. In terms of dollars, Belgian export price index was 261, while Britain's was 182. The total yields from Belgian exports were only slightly less than Britain's. "The Belgians earned as much in foreign exchange while keeping their goods at home to add to home consumption instead of exporting them." The obvious signs of prosperity in Belgium were "due mainly to better planning of the foreign exchange rate."

The writer asserts that if the pound had been put 25% higher in 1945, Britain would have saved about £600 million of gold in foreign exchange. It does not mean that appreciation is always the best policy; in the twenties it was not. In Ceylon, appreciation was possibly preferable during the last five or six years and may continue to be so for some time to come. Later, it may be necessary to plan the rate differently. The important point to remember is that "following simple rules of exchange manipulation"<sup>2</sup> may often render an already difficult task more difficult. It is possible that Ceylon's development programme under the Colombo Plan would have benefitted more by not joining in the general devaluations in the Sterling Area in 1949.

---

1. Lewis *ibid* Page 68.

2. Page 69.



### Inducements to Investment

Next, an aspect of financial policy akin to more traditional monetary problems may be mentioned. It is almost an axiom for us that the maximum possible saving consistent with certain consumption standards should be found internally. The problem is mainly one of tackling the question of liquidity. Large hoards could exist but remain useless for the country's economic development. It is in this category that the well known inducements to capital to come out and invest fall. The relief afforded on taxation, the allowances on depreciation and several others are really attempts to break the seclusion of these hoards—although, to some extent, they are set-off by low profits, or high-priced capital goods, labour and other factors. On this subject of taxation and capital formation we may, in passing, make a recommendation which should become a pivotal point round which all other such measures may be built. It is the exemption of those Company Receipts (over and above depreciation etc.) that go into investment (and not just reserves) from taxation; or imposition on them of favourable differential taxation.<sup>1</sup> So that if the entrepreneur does not want to contribute to further investment, the tax becomes legitimate. If wage-demands rise the State can reduce the tax, or if the stage has been reached when capital formation could really be slowed down, the State could instruct diversion of part of this new 'investment' into the wages Bill.

To continue our point about maximum internal savings,—it is the task of the banking system and in particular the Central Bank to look after liquidity and to control interest-rates by regulating supply of money. The failure of the monetary authorities to fulfil this task, or defects in the machinery through which savings are made available to industry may hinder the development of existing resources.<sup>2</sup> Where this is the case internal reform rather

1. An alternative method is to tax e.g. all Estate Profits above a certain amount, and invest them in industrial corporations giving the tax payers the right to be shareholders in the concern. It must be remembered also that Estates benefit already from Government by wage rates being held in check by the Government's extensive policy of subsidies on rice etc.

2. "The main symptom for such defects is the high level of interest rates. The history of industrialisation shows that these can be reduced in a fairly short time by means of monetary and financial policy. See, e.g. the rapid reduction in interest rates in Japan in the seventies and eighties, described by Shigeto Tsuru (*Economic Fluctuations in Japan, 1868-93*)<sup>12</sup>—Mandelbaum, loc cit Page 9.



than external financial assistance is indicated. The purpose of the latter is to reduce a genuine scarcity of home resources by enabling the industrialising country to draw upon the resources of the outside world. Loans therefore should be given and used exclusively for payments abroad to purchase foreign equipment and raw material or to finance imports of essential consumer goods. If it is the last the purpose would be to free domestic resources "more easily for Capital formation. Loaned funds which accrue to Central Bank reserves or are dissipated in the financing of un-essential imports do not increase the productive capacity of the debtor country. More often than not they result in default but even if their servicing is possible it causes a fall in the real income of the borrowing country as its capacity to produce income has not increased *pari passu* with loans received."<sup>1</sup>

### Wages

On the question of Wages several problems exist. On the levels to which, in a given situation, wages could rise, there is first the problem of the elementary quantity theory relationship and of inflation if its tenets are discarded; further, though to talk of a Wages Fund in the crude sense would be incorrect, it is true that the country could consume only what is actually produced. At a lower level, i.e. in the industrial Unit, the relationship between wages and profitability is true; and true not only to enable continuation of existing capacity but ensure future investments. Of course, it is both incorrect and unfair to treat remuneration to all other factors as residuary and wages alone as the cause of high cost. It will have been noticed that the call for land reform, for a correct central bank policy and adequate skill—to mention some of the major items—is really based on the damage that the failure in these could do to successful development. It would be accepted, however, that at a given time the general level of wages cannot be varied to suit extreme desires.

But wages in the several sectors of the economy could vary and it will be natural for them to do so. Generally speaking the principle of determination would be related to the only two relevant considerations, viz. the 'standard of living'<sup>2</sup> and the capacity of the

1. Mandelbaum, Page 9

2. Striking results have been claimed in the U. S. A. from giving workers a fixed share of sales. This is naturally tied to a system of practically fixed wages—which may be taken to correspond to our 'standard of living' wage. Lewis *ibid* page 90-1.



industry to pay. But in the dispute between standard of living and capacity of industry, the latter must be accorded, at its own level, undisputed consideration. The difference must be met by tying up, wherever justified, the policies of subsidies to 'high-cost' industries by the State. It will be noticed that the subsidies (discussed earlier) will be not at finished-product but at factor level.<sup>1</sup>

It is the failure of policy to enable planned National Output to be consumed that is reprehensible and illustrative of the curse of poverty in plenty. Not to put out money with a view to consuming what has not been produced is certainly not failure of policy—so long as it is true that the best possible production programme is really in operation.

### Prices

It is also evident that a wages policy can be spoken of as satisfactory only in the face of an already accepted prices policy. Fair

---

1. On Russian experience there is the statement that (in real terms) "this is identical with the decision about the amount of resources to be devoted to the consumer goods industry." But "it became the practice for a general wages policy, defining the general contours of the wage structure, to be agreed upon annually between the Central Council of Trade Unions and the highest organs of government in the economic system." So that the intervention of trade unions must take place then "and not in the form of subsequent bargains." The Unions were to secure in the course of dispute at lower levels only "such improvements as are compatible with the economic development of the worker's State and are without injury to other sections of work people."—Dobb, Pages 309, 310, 316.

c.f. the following from the British White Paper on Employment Policy (1944) "There must always be room for the adjustment of wages and conditions, e.g. on account of changes in the form, method or the volume of production. Also there must be opportunity for the removal of anomalies in the rate of remuneration of different grades and categories of workers, both within an industry and between different industries. The principle of stability does mean, however, that increases in the general level of wage-rates must be related to increased productivity due to increased efficiency and effort.

"An undue increase in prices due to causes other than wages might similarly frustrate action taken by the Government to maintain employment. If, for example, the manufacturers in a particular industry were in a ring for the purpose of raising prices, additional money made available by Government action for the purpose of maintaining employment might simply be absorbed in increased profit margins and no increase in employment would result. Stability of wages and stability of prices are inextricably connected. If the general level of wage-rate rises, and there is a corresponding increase in prices of goods for civilian consumption, the individual wage-earners will be no better off and there may be no increase in the total amount of employment available."

The subject of Planning may one day come to be written as the story of how familiar economic realities do make the practices equally in what are acknowledged to be vitally divergent systems.



prices is a crucial term. It is responsible not only for the satisfaction of labour with a given policy on wage levels, but also for the continuation of investment and output by Capital. The possible contradiction is that with labour wanting low prices and capital wanting high prices (relatively to Wages Bill) fair prices may go by the board. Fair prices certainly must not be near high levels. But how low they should be depends on a joint reckoning based on profitability of output and the subsidies (referred to previously) by the State to certain industries. The interest of Capital in high prices is, of course, for final consumption goods, and not for goods at higher levels consumed by industries themselves in the course of production. In itself this outlook is unfair. It need not really exist for continued production, so long as legitimate profit is added on to selling prices. But several 'frictional' forces repeatedly upset cost and price calculations to entrepreneurs. For that reason, the general expectation of rising price levels, and not falling, nor even stationary, is implicitly put forward as a condition for development. It is a point round which much discussion on trade cycle theory has taken place—of which the argument of 'neutral money' versus 'price stabilisation' is the nearest related to our discussion. We cannot pursue this here but we shall have something to say in a more appropriate context in the chapter after the next.

### **Selling**

A few observations are necessary on the ensuring of consumption. Once the Development Programme is decided on, there is one point on which the planning authority should be clear; that is not to hesitate to go to the aid of actual selling in order to eliminate no-selling (or weak-selling). So that not only should an adequate money volume be ensured by the budget, but every assistance rendered to actual consumption. Sales Societies, Marketing Organisations and Purchase Organisations to contact producers especially the Cottage and (Rural) must be ensured. There is, and should be, no attempt at 'dictation' of consumption. What is important is that surpluses should not be false frictional surpluses



and the producer must not languish for want of selling intelligence and organisation or facilities.

### **Dynamic Economics**

Before we leave the subject of Planning, we should remind ourselves of our earlier references to the inadequacy of accepted full employment devices in the context of dynamic theory and conditions. The economics we are concerned with is in the fullest sense the Economics of Expansion. It is very clear that the whole structure of the Plan would be based and reared on a foundation whose entire range of existing dynamic forces is fully reckoned. There is the point by Keynes, for instance, in the *General Theory* that the duration of capital assets varies according as the population is increasing or decreasing; or Harrod's, that in the great era of expansion in Britain the population increase alone probably entailed a requirement for saving of some 6% of income and that "another sizeable fraction went away in overseas investment."<sup>1</sup> There is again the case we referred to of the agricultural development programmes in Ceylon leaving the country in the same relative state of food deficiency at the end of six years because of the increasing population. Yet again, the finance of education, social security and certain health policies are contingent on the population compositions of the future. The relationship between Investment and Consumption in the Plan will be vitally dependent on the dynamic factors—for, in the language of Harrod, there is a rate of growth of  $G$  which is fundamental to a dynamic economy. A series of instantaneous pictures over the next, say, 20 years, is no substitute for a decision on capital investment now in terms of what the call on it will be 10 or 15 or more years hence. A planned increase of output shows itself years later only and then the trend of demand may be different. "The notion that successful development from one economic situation, with its given combination of resources and configuration of demand, to another might be a

---

1. Towards a Dynamic Economics, Page 130.



more crucial test of the contribution made by an economic system to human welfare than the attainment of perfect equilibrium in any given situation seldom commanded attention."<sup>1, 2</sup>

The foregoing brief discussions do not cover the whole range of problems under Planning. Yet, for the purpose of our Study of full employment, we should now know enough to be able to "fill in the details". What is more important for the thesis is that what we have said sufficiently establishes the case for planning in the policy for full employment.

### Some Estimates of Costs

Finally and as an epilogue to this Chapter, it would be interesting, in broad outline, to assess the magnitudes of the task that would be involved in particular countries under a scheme of planned development for Full Employment. Of course, short of preparing an actual plan there is no fully satisfactory manner of estimating the total cost of development. It is, however, possible in broad outline to follow the method of Planning and by estimating the minimum standard of food, living and other requirements, for the whole population, to subtract the quantity of the existing amount thereof and finally work out how much capital investment the difference would involve. The Bombay Plan is an attempt on these lines. Such a method would really require a group of people to probe into and collect all data adequately—the best result being obtained only with a body of Governmental proportions. The other method of estimating the cost would be to estimate first the total surplus labour in the country, and work out correspondingly total capital

1. Dobb, Page 3. This is also evident in recent American discussions. c.f. recent Annual Papers and Proceedings of the American Economic Association, published in the American Economic Review, especially 1950 onwards. e.g. the papers by Singer (1950), Nurkse and Adler (1952).

2. As a representative instance of an essay in dynamic planning may be mentioned the Monnet Plan of 1947 for France. With a real national income in 1939 of about the same only as in 1913 and capital equipment averaging 25 years against 7—9 in Britain and 5—7 in the U. S. and the average age of dwellings 50 years in the town and 100 in the country, the Planning Commissariat worked out its plan to reverse the trend. Certain industries were classed into the basic category—coal, electric power, steel, cement, agricultural machinery and transport. Later, agriculture, oil and fertilizers were elevated to this category. The bulk of the investment has gone into the electric power industry and agriculture. One conclusion apparently endorsed in the course of implementation was that "if left to its own devices French industry would very probably have slid down the slope of decadence." In the field of financing the significant conclusion seems also to have been brought out clearly, that "modernisation should finance itself"—in other words, then, that initial development has its own momentum for future expansion.—Economist, February 4th, 1950, pages 269-70. Also of June, 1948 page 1020.



required to absorb that entire surplus. Estimating Capital Investment per head has been somewhat simplified as a result of various studies and this latter method would appear to suit attempts at estimates of costs by individual students very much more. It will be noticed that the former is meant directly to produce the required output while the latter is meant to absorb total labour. Actually, both the devices could be made to be mutually helpful; by adjusting the Capital Investment Programme under the former if that still leaves numbers un-employed, or by increasing Capital Investment under the latter if the original estimate does not still produce the required volume of goods in relation to the standard of living.<sup>1</sup> Without digressing too far on this subject we shall mention some estimates made for economic development.

(a) The Bombay Plan is well known. But quite an interesting analysis for India made about the same time may be reproduced especially in view of its approach to the estimates on Agricultural Development.<sup>2</sup> "Quite unscientific as the estimates of prior debt on agricultural land in India are, a tentative financial long term estimate should be somewhat as follows :

	In crores of Rupees
'The total debt directly or indirectly secured by agricultural land in the whole of India (including Indian States) ... ..	1,750
Big cases which should be left to themselves—say over Rs. 15,000 debt in each case ...	450
Good cases requiring no extraneous aid—out of Rs. 1,300 crores (leaving out big cases) ...	300
Out of the balance of Rs. 1,000 crores hopeless cases which must be sold out may amount to ... ..	250

1. Vide top of Page 231 above.

2. Economic Journal, June-September, 1944, Page 197, et seq.



	In crores of Rupees
The remaining Rs. 750 could be easily scaled down to ... ..	400
Add— for crop financing in the cases ratio- nalised ... ..	100
Add further—for other long term purposes constituting land improvement, irrigation, hydro- electric power, machinery, artificial manures etc. ... ..	500

The real problem is therefore of the order of Rs. 1,000 crores. A scheme proposing to cover one tenth of this figure in the course of ten years should prove quite successful in solving the problem of agricultural finance in India. That is to say if land mortgage loans could be rationalised at Rs. 10 crores a year for ten years the remaining cases still with money lenders should automatically become rationalised in view of the model set (compare the fact that one of the greatest uses of the co-operative Credit Movement in India has been the reduction of the general rate of interest in villages *outside* the societies); further the Rs. 100 crores paid out to the money lenders must again enter the field of investment either in the shape of new money lending business by the money lenders themselves or through co-operative institutions in which the funds should find a place as deposits. Or the money may go to finance new industries. In any case Rs. 10 crores a year for ten years should be quite large enough provision for facing long term finance problems."

At the next stage, a zero programme of development is worked out and is as follows :

	In crores of Rupees
Agriculture—rationalisation of prior debt or land and modernising (keeping the small hold- ing intact) including items like irrigation and hydro-electric works, initial manuring, embank- ments, enclosures, etc. ... ..	1,000



	In crores of Rupees
Clothing and other consumption goods industries—mostly through small scale and cottage methods ... ..	400
Housing—there are about 8 crores of families. Assuming that half the number are already provided at Rs. 100 per capita outlay ...	2,000
Education—Universal Elementary Education (adult, vocational, technical etc.) at Rs. 50 per pupil for about 160 million pupils ...	800
Health and Sanitation—at Rs. 20 per head ...	800
Means of Communication—transport defence (initial quota) etc. (including miscellaneous items) ... ..	1,000
Total additional capital outlay required initially ... ..	6,000

Spread over ten years this would entail an investment of 600 crores per annum or about ten per cent of the National Income which could be put at 6,000 crores per annum?

The total cost of the Bombay Plan is estimated to be Rs. 10,000 crores spread over 15 years.<sup>1</sup>

(b) In another context, it has been estimated that a capital co-efficient in relation to income of 3.9<sup>2</sup> obtained in the U.S.A. in 1929. It means that the annual national income multiplied

1. The Official Five Year Plan for India, finalised at the end of 1952, was not available at time of writing this chapter. Reviews of the Plan immediately following its publication credit the Bombay Plan with more realism that it was possible at one time to invest it with. (c.f. especially issues of Eastern Economist).

2. Industrialisation and Foreign Trade, pages 47-48.



by 3.9 gives the total capital existing in the given state of capital development. For a Plan of development for India or Ceylon, we may assume a similar coefficient as the largest necessary. Another co-efficient, of 2, has been given by Dr. Lokanathan.<sup>1</sup> These could really be taken as representing roughly the extreme limits on either side and the annual output as being somewhere between  $\frac{1}{4}$  and  $\frac{1}{2}$  the capital invested. The former fraction is not likely to be lowered (despite relative inefficiency in methods and skill) because of the overwhelming application of labour to each unit of capital and the second fraction is not likely to be exceeded because of the high capital consumption in various 'services'. For example, the co-efficient for electric light, power and gas in the U.S. in 1929 was estimated at 12.2, and even if it should be lower in our case it is yet likely to be very high.

(c) For an example along the second lines, i.e. in relation to surplus labour, the two points involved are decisions on the particular capital investment figure per head, and the actual surplus labour.<sup>2</sup> The various industries (agricultural and industrial) may be classified as follows viz., (1) Light, (2) Medium or (3) Heavy.<sup>3</sup> We are informed that the capital equipment per head in respect of each may be taken to be (1) £100—£400; (2) £400—£800; and (3) £800—£1,500 (pre-war prices). We may immediately remark that the industrial Policy in Ceylon must contemplate only industries in the first class.

On the question of the actual figure to adopt, we may provisionally adopt £300 per head, as an "averaging out" after considering necessary expenditures on hydro-electric production, roads, railways, building and similar heavy items. Before accepting this however, we would have at least to double the figure to £600, to allow for the present level of prices. Regarding the estimate of

1. Eastern Economist, pamphlet No. 1.

2. One interesting example of this sort is the Central Economic Plan for 1950 of the Netherlands. The plan runs in terms of Means and Needs. The amount of the National products is determined by the size of the working population—which is fixed at as high a number as is practically possible—and the output per worker. The division of working population into the various sectors is given at the bottom of next page. c.f. Eastern Economist, January 6th 1950, Pages 20-1.

3. Economic Journal, June-September, 1943. c.f. also American Economic Review, May, 1952, page 508, Simon Kuznets—"Proportion of Capital Formation to National Product."



surplus labour, it has been stated for the Balkan countries that the surplus labour (active) is  $\frac{1}{7}$  the total population of 42,000,000 (1945). We may, hypothetically, assume a similar proportion as applicable to a country like Ceylon. On this basis, and assuming our population to be 7 million, we get a surplus of active labour amounting to 1 million (inclusive of under-employed). On this estimate we should get the figure of about Rs. 8,000 million as the cost of a plan for Ceylon ( $\text{£}600 \times 1 \text{ million} = \text{£}600 \text{ million} = \text{Rs. } 8,000 \text{ million}$ , approximately). Taking the capital co-efficient (vide previous paragraph) to be between  $\frac{1}{4}$  and  $\frac{1}{2}$ , we may estimate that the national income, which was nearly Rs. 4,500 million in 1951, will be between Rs. 6,500 million and Rs. 8,500 million (at 1951 prices) when the plan is complete ( $\text{Rs. } 4,500 + \frac{1}{4} \text{ Rs. } 8,000 = \text{Rs. } 6,500 \text{ million}$ ;  $\text{Rs. } 4,500 + \frac{1}{2} \text{ Rs. } 8,000 = \text{Rs. } 8,500 \text{ million}$ ).

The period within which the Plan would be fulfilled may be worked out in terms of the rate of investment envisaged. At the Russian rate of investment which was  $18\%<sup>1</sup>$  of the national income an annual investment of Rs. 810 million should be feasible (through loans or savings, including depreciation and provision against

(In thousands)

	1948	1949
Industry ... ..	1,395	1,415
Agriculture ... ..	565	565
Trade, transport, banks and other services ... ..	1,250	1,250
Education ... ..	104	105
Civil Service ... ..	215	205
Military Service ... ..	169	169
	<hr/> 3,698	<hr/> 3,709

1. c.f. Dobb, Page 290, "investment and defence combined probably swallowed about a half of the national income in the year before the U. S. S. R. entered the War."



reserves as well as taxation) and the Plan itself will take about 10 years to complete. On the other hand, foreign borrowing and reserves like sterling balances have not been considered. This should shorten the period of the Plan conspicuously. As the Plan proceeds and incomes increase, the constant rate of saving<sup>1</sup> should produce more than Rs. 810 million investment a year.

If, however, the 18% is only an average over the entire period, with the initial rate less and the latter rate more than the average, the period of the plan does not get affected. Assuming what is probably a more likely rate of investment, namely 12%, an annual rate of Rs. 540 million will be the investment and the period of the Plan will be about 15 years—again of course considerably reduced by foreign borrowing, Capital balances and so forth. As both saving capacity and borrowing power are dependent on maintenance of prosperous economic conditions generally, it is safer to assume a 15-year period as the more appropriate. This is also necessitated by the fact that the total investment figure is computed on present population and no allowance is made for increases in population. The capacity to borrow abroad, or to save (as development proceeds) more than an average of 12% of Income, may be set off considerably by the population increase. It may also be said that the apportioning of the finances among taxation, savings, capital borrowing and creation of new money will depend partly on the time within which it is desired to complete the transition.<sup>2</sup>

---

1. The point is often emphasised and needs to be appreciated that a state of development is the best answer for further development as well as for automatic multiplying of the national product. One of the best indices for appreciating that point would be the fact that company appropriations on depreciation and reserves constitute really the bulk of investment volume in advanced economies, the public sector and private savings coming only second to this. This point, that development after a time contains its own motive energies, was recognised clearly in the Monnet Plan. c.f. endorsement of the point also in American Economic Review, May 1952, Adler, page 593, Fiscal and Monetary Implications of Development Programmes.

2. There are also vital factors like productivity—e.g. installed capacity at peak level can carry the Indian index to 143—about 30% above existing production—Eastern Economist, October 21st, 1949, Page 604.



(d) An interesting estimate made for India,<sup>1</sup> is worthy of repetition at some length. "It appears from the figures of investment and savings before the War that we were investing and saving at a net rate of about 1% per annum for the 20 years preceding. In the Eastern Economist of October, 1948, Colin Clark on the basis of certain estimates of investment, gave the following interesting figures for Indian investment and saving in terms of international units. An international unit is really a measuring rod of income of which one unit is equivalent to the volume of goods and services which one dollar would have purchased in the decade 1925-34 in the United States.

### Indian Investment and Saving

(Thousand million I. U. per annum.)

	1919-23	1924-28	1929-33	1934-38
Railways, industry and mining	0.48	0.44	0.19	0.20
Other investment	1.40	1.59	1.70	2.40
Balance of payments	- 0.18	- 0.03	- 0.08	- 0.09
Total savings	1.79	2.06	1.81	2.51
I. U. per head of occupied population	22.4	24.5	20.6	27.1

1. Eastern Economist, 1948, Annual Page 1132 et seq. It may be mentioned that there is no dearth of estimates. e.g. Eastern Economist, January 27th, 1950 Page 130, where a rate of saving of 6-8% is deduced starting from the case of the cotton industry. c.f. Eastern Economist, March 3rd, 1950, Page 331, where the point that India's population is not increasing so fast is mentioned and the concept of non-monetary investment in agriculture is also brought in.



Into the details of these calculations it is not necessary to enter. But as far as we have been able to ascertain, they do not differ markedly from estimates which we have made . . . and it may be assumed that as a description of the past they indicate correctly the order of magnitudes involved.

Since we have in effect kept our standard of life fairly constant the conclusion must be that our pre-War rate of savings and investment kept us over the long period maintaining a rate of advance of about 1% per annum in net production. At pre-War prices, Colin Clark's figures for annual investment in each of the four quinquennial periods up to 1938 were Rs. 150 crores for 1919-23, Rs. 140 crores for 1924-28, Rs. 114 crores in 1929-33 and Rs. 139 crores in 1934-38. Our own calculations for the rate of savings in subsequent years computed for different years of the War indicate a higher rate of savings than before the War. Apparently in 1939 we were saving 9% of the income while in 1941-2 we actually reached what seems to be an all-time high of 18.5%. We have now declined somewhere near zero and our pre-War rate of advance of about 1% per annum on net production has been converted into a rate of decline at the same rate. But the fact that in spite of the great poverty of our people, we were able to maintain the relatively high rate of pre-War investment and that we could reach as high a figure as 18.5% during 1941-2 shows that there is great ground for hope.

The wonderful example of Japan between 1908-1924 shows how a poor country can build up a remarkable rate in spite of poverty. We cannot emulate Japan's peak figure of 55%, but we have gone near enough her average of about 21%. But it is clear we will need a Herculean effort to get back to the peak 1941-2 level."

"Nothing but the most drastic insistence on economy in private as well as in public life will serve to reverse the position of dis-saving and convert it into a position of net saving of the order of Rs. 500 crores per year which is required at present prices to maintain our standard of life. To double national income per head in 15 years from now we will need expenditure of a much larger order. Opinions differ considerably on the rate of saving and investment required. Mr. Colin Clark considers that the rate of capital per



worker will need to double if we are to succeed in attaining in 17 years the net advance of productivity of 2% per annum. Mr. G. D. Birla who regards the matter in terms of the short period of the next 5 years, assumes a far smaller capital-income ratio. Their differences are explained by the consideration that Mr. Clark works on the basis of the unhappy past and tends to be as pessimistic as the figures he examines while Mr. Birla working more on theoretical possibilities has erred possibly on the other side. There is no doubt that theoretically we can make much greater use of the capital which we have—for example by triple shifting throughout our textile industry as Mr. Birla suggests. But in point of fact we are not triple shifting in this industry so that this new income and the net saving which would have resulted if this had been done, are not created.

“It is not possible at this time, with the very inadequate data, to estimate with any precision the net investment required under Indian conditions to double the per capita national income of India in 15 years. It is probable, however, that Rs. 30,000 crores at present prices is the minimum for capital expenditure under all heads of public and private account. This is far more exacting than the target of the Bombay planners whose Rs. 10,000 crores at pre-War prices included much known capital expenditure. It is certain now that the authors of the Bombay Plan who expected a five fold increase in industry in 15 years from an expenditure of Rs. 4,480 crores at pre-War prices were unduly optimistic; they were both technically and financially optimistic in expecting from an expenditure of Rs. 1,240 crores 130% increase in agricultural output. New and better Plans will need now to be made with the greater data which are available.”

As we said, the framing of such estimates, however near the mark, is no substitute for actual planning. But they are very useful and serve a purpose in imparting a sense of proportion to our general economic aims and thinking on which we naturally depend.



**PART IV**







## CHAPTER THIRTEEN

# Internal Full Employment and World Economy

(i)

THE state of full employment resulting from the policies previously outlined is bound to bear the impress of several marked and beneficial characteristics. The underlying and fundamental characteristic will be the emergence of full employment, accompanied by an increase in the total quantum of national wealth. This increased wealth will have been occasioned by the import of capital equipment as well as the exploitation of internal resources. Yet, the employment is 'full' only at a postulated minimal standard of living. The scope for raising the standard further will still exist. The ability to exploit this scope is best observed from the angle of the balance of trade. For one thing, the balance of payments position is no longer determined by the absolute necessity to import wage-goods. The latter being intimately related to propensity to consume, the implications for social and economic policy become immediately clear. The basis for creation of much that is essential to national wealth and living standards now exists. The construction of houses, the provision of recreational and allied welfare services as well as the more ambitious aspects of Social insurance and security, including Free Education, will add to purchasing power and thereby raise consumption levels; but they would simultaneously stimulate internal production activity and not, as before, the volume of imports.

The importance of it, socially, can be neither over-rated nor too strongly emphasised. For the stage is set at last for the ultimate realisation of all the facilities and enjoyments of a high and rising standard of living.

Accompanying and buttressing this central benefit are also certain other prominent characteristics. A chronic threat to the balance of payments is no longer unavoidable. It is not a



thing that has to be watched unhelpfully and without power of rectification save by outside circumstances and factors. There would be several reasons for saying this. A falling return from exports could previously not have been met by any drastic cutting of imports save at the risk of starvation and possible famine. Under the new set-up, the imports would either be capital goods, or consumption goods predominantly of a luxury or semi-luxury variety. The former could much more easily be curtailed during a time of depression in the export industries than could wage-goods, and the second could be restricted to a large extent not only with much more justice but also much less deleterious effects on the economy. Further, the previous inelasticity of demand for imports will cease to exist. It does not thereby eliminate such inelasticity of demand (and of supply) as may obtain for the agricultural exports. Yet, the vastly improved bargaining position of these countries under the new set-up is bound, both through the various marketing devices and the terms of trade, to obtain a markedly better return than would otherwise have been possible and to impart to these governments a greater ability to deal with adverse balances in the payments.

( ii )

While the foregoing are logical deductions from the economic policy envisaged, they may be too rosy to be completely true. In spite of our copious references to the balance of payments and import of capital etc., we have so far been more or less confining ourselves to a 'closed' economy. There are some external influences which even a diversified economy must confront. It is not the purpose in this thesis to go into the question of the contagiousness of the trade cycle; nor into the mass of historical evidence that has now led to the acceptance of the dictum that "full employment, like peace, is indivisible." The principles of international economic equilibrium need however to be briefly observed. The principle of automatism and laissez-faire had, in reality, probably longer currency in the sphere of international trade than in internal economic activity. It may be true to say that not till BRETTON WOODS did theories of the automatism of gold as international currency and of undiluted free trade cease to be actively sponsored as universally valid. The assumptions on which the twin theories



were based—those of a balance in the payments and of full employment—could have been tacitly assumed away during the periods of 19th century expansion. But, in the seriously disjointed circumstances of the recent decades, they had to be brought into the forum for thrashing out, since failure to do so would have amounted to a begging of the entire question.

The general result of this academic movement was the evolution of a system calculated to ensure full employment at home, as far as practicable insulate the internal economy from the infections of any trade cycle abroad, and to effect, in the long period at any rate, a balance in the payments of all countries. The practical fruits of this trend of thinking were the International Monetary Fund and the World Bank; the former built on the two pillars of efficiency wage levels and flexible exchanges and the latter on the sane recognition of the point that "it is impossible to maintain an international monetary system except on the basis of an international economic system."<sup>1</sup> The theoretical advantages of both these institutions are undeniable and they obtain equally for industrial and agricultural countries.

What is more of concern to us now is the inadequacy of even this mechanism in certain circumstances of world production and trade. On the side of the agricultural countries there is the inadequacy of the resources that the World Bank can lay at their disposal today. It calls at once for clear cut action based, either on surplus countries stepping into the breach with sufficient capital, or on the countries affected working out a 'regional' as opposed to a global system of trade and production. The industrial countries that have been under-going difficulties since the War will also need large capital assistance programmes.

While the assistance is on there may be no difficulties. But the same capital loans can become mill-stones round their necks in the entirely altered climate they would be facing some time later, of almost nil invisible earnings and a regular programme of repayments of capital and interest. Then we have a situation where, even after a diversification of the agricultural countries, the latter will have to be partners in the general misery of a falling

---

1. Gregory—"The Gold Standard and its Future."



world trade. They will be depressed in respect of their internal living standards as well. (We may interpose here that this depressing influence is not to be confused with their present experiences when they have, in addition, no internal wage-goods industries to set-off external effects even partly). To that extent, internal full employment does not still achieve its object and it becomes even more important that the international arrangements should be also of the best possible pattern.

Before we proceed to that, the chief implications of the theory of international economic equilibrium may be set down. In brief, it would be as follows<sup>1</sup> "If within the provisions of a multi-lateral system still the deficit limits are reached, then the overdrawn countries might have to be rationed by direct intervention and thus far it would be a degeneracy into some form of Bilateralism. Escape from this is possible. But what is the nature of such escape? Deficit countries might be given a loan, failing that, a devaluation of the currency might be the best, and failing that, some fundamental readjustments in the internal structure of production are called for. The granting of loans is the easiest, but they are sound only in cases of genuine economic development. To repeat, international capital movements always are and must be an exchange of import surpluses today against export surpluses in the future—and sound therefore where the debtor can increase its future capacity to export by increasing its current imports. Devaluation itself has its strict limitations. Broadly it is successful only if it is a case of adjustment away from an abnormal position in order to correspond to the other norms, of the quantity of trade, the volume of money, the wage level, efficiency etc. Under no other circumstances does it provide an ultimate solution. In this connection, we may note that while 'each nation should be free to do internally whatever it pleases . . .' and while 'its responsibility to the rest of the world should end when it has balanced its Clearing Fund Accounts', the two are too strongly interconnected to be treated as entirely separate. Some of the national policies may be perfectly compatible (and advisable) with such an expansionist international system as we have in mind, but some others will certainly be quite inconsistent with it. The primary responsibility should rest on the shoulders of surplus countries to spend as much as they

---

1. My "Ceylon, Beveridge and Bretton Woods" Pages 8-9.



have earned; and a secondary responsibility should rest on the shoulders of the deficit countries to make available at the right prices etc., a sufficient volume of goods so that all cash obligations can be discharged in kind.' Hitherto we were faced rather with the anomalous position where just those who could buy more (surplus countries) bought less (relatively) while those who had to buy less were made to buy more. Finally, failing the first two, or when those two are inadvisable the third is the solution which is probably indicated. So we are reduced to the position that while after a point surplus countries must import, if they desire to export; while an enlightened International System will give the 'expansionist' fillip to trade; while more backward (economically) countries might have ample scope especially in the shape of the deficit allowed and additional loans; while pegging of the exchanges at a wrong level may not be treated as irrevocable; while the fortunes of countries may no longer be fatefully dependent on their uncertain stocks of gold; while a wage system properly related to efficiency is given its right to remain untampered with—still, since it is true that anything bought must ultimately be paid for and since it follows that no international system however clever can get behind such truism, therefore it remains that multi-lateral clearing is ultimately possible, only under sound planning and rational organisation of the economic structures of countries."

One thing may immediately be said. The international monetary system, the principle of multi-lateralism, and even the rationale of a World Bank are conceived fundamentally in terms of the ultimate viability of the economies of the world within the framework built up by those trends of thinking.<sup>1</sup> It is also recognised therefore that the transitional interval (which could be quite long in fact) for several countries is one of non-viability; and so, several of the features of the international monetary system will have to be suspended till the substance of the international economic system has been built up. We have had occasion previously to discuss free trade and protection but one development of it in the international sphere calls for mention. The Havana Charter was a well meaning attempt and its motives certainly indisputable. Nor could it be said to have been entirely unrelated to the realities of the situation; for, clearly, one of the specific exceptions it makes

---

1. Free Trade and Convertibility, we may emphasise, are allied.



to its fundamental philosophy of low tariffs and freer trade is the case of the under-developed countries and their policies for nascent development projects. It takes away a good portion of the facilities conferred by the one hand, however, through the institution of somewhat involved procedure before a country could obtain the necessary sanction from others for protection in terms of the relevant concessionary clause.

The Ceylon Industrial Products Bill (requiring purchase of a given proportion internally for certain items of industrial products imported) which came at Annecy for approval and went through not after little delay and anxiety is, probably, a case in point. But a more important criticism of the Havana Charter would appear to be its overlooking of the point that an important problem to which it had to give consideration was the chronic adverse balances of payments of several countries. The liberalising of tariffs by countries disadvantageously placed was less easy and their use of them could be even justified; while, on the other side, a liberalising by surplus countries would be both easier and far more obligatory. If so the whole scheme of tariff policy and reduction should have been worked out in terms of the balance of payments positions and prospects of the countries, and not (as has now been done) in terms of the number of concessions granted by one country to another.<sup>1</sup>

( iii )

In pursuing the subject further, we may remind ourselves of the earlier statement that to the extent that internal full employment does not achieve its object it becomes even more important that the international arrangements should be also of the best possible pattern.

A chronic adverse balance of payments in the developed countries or a general internal depression in them, would, in either case, curtail imports from the agricultural countries (either quantitatively or through lower prices). Internal depression need not be considered a possibility within these economies (of West Europe).

---

1. In this c.f. Henderson in the A. E. R., 1949, through which the clearer expression of the idea has been facilitated even though it was not originally taken hence.



The chief danger to the stability of the agricultural countries would be through the present chronic adverse balances of the former and the inevitable restrictionist policies entailed. It is this feature that would appear to call for special comment and assessment. Apart from the War-time devastation and the neglect of capital creation and (if viewed in perspective) probably even more prominently than that, two features stand out as responsible for the immense struggle of the industrial economies of Europe for viability. First, the whole structure of the standard of living had proceeded on the assumption of a considerable quantum of invisible exports,<sup>1</sup> which for our purposes may be called return from foreign investments. The devastation of those colonial countries where the investments were held, the expenses of war that entailed selling out of large investments in other foreign countries, and partly the emergence of balances held by colonial and semi-colonial countries against the former overwhelmingly creditor countries, not merely imposed a strain but upset all the calculations on which the industrial countries had hitherto worked in considering their strength or their abilities. It would probably have been yet a fact to say that viability could have been easily reached, if that were the only obstacle. The second fact which has been probably more responsible, although it does not appear to have been as much admitted or mentioned is the break up of Europe as an economic unit into two parts.<sup>2</sup> It seems very likely that a continuance of the pre-war integration (economically) of East and West Europe and their complementary functioning would have solved the practical riddle of conspicuously

1. Probably one of the most spectacular evidence of the change was the deal with Argentina in which the whole capital assets of the British-owned railways was bartered away for 18 months' meat. *Economist*, February 4th, 1948, Page 249.

2. Swatantra, January 31st, 1948, Page 29. "The sixteen West-European nations which gathered at Paris last year to draw up their plan for survival, regarded it as fundamental to the achievement of their objective that trade between the western and eastern parts of Europe should be not only continued but developed further....At the present moment there are as many as 48 trade agreements between West European and East European countries. In addition the Anglo-American bi-zonal authorities in Germany have commercial agreements with five countries of Eastern Europe....If in the process of implementing the Marshall Plan, the Marshallled countries should be curtained off from the Stalinised countries the resulting dislocation of European economy will be disastrous for all concerned...."c.f. also *Economist*. September 18th, 1948, Pages 446-47, for a general analysis. Also October 16th, 1948, Pages 634-5 in which attention is drawn to another related feature in prewar trade, viz. the large exports of fruit, vegetables and livestock products from Western Europe to Britain. Yet another point was that Germany's pre-war trade with Western Europe was larger than that of any other European nation, Britain included. It was a fifth of total



higher levels of productivity in relation to pre-war (e.g. in Great Britain) and the co-existing intractability of the balance of payments situation. It is in fact neither the quantitative magnitude of production nor of export goods but that magnitude comprising the right composition of goods that is important. Nor is it an unknown fact. For one industrial country to be able to pay back for enormous agricultural imports from another more industrial country with industrial produce is, even under favourable circumstances, a difficult and arduous task. The sales resistance (relatively) of the American consumer for imports is understandable and economically rational. On the other hand, there are at least two reasons why exports to Eastern Europe, if most of the food stuffs were imported from there should be far easier. Firstly, the demand for industrial products per se is there, and secondly, the export of precision goods has not the same possibility of meeting alternative home produced goods. Of course, so long as the present economic separation of East Europe exists that is no solution; though it brings out clearly the difference to Western Europe by the change from the pre-war position.

It would seem, however, that any attempts to reach viability by concentration on exports to the U.S.A. are bound to fail. If they do, the repercussions will be serious for the agricultural countries as well.<sup>1</sup>

It would appear far better if the above system of 'regionalism' into which the economies have strayed, by reacting almost mechanically, were over-ridden or replaced by some form of what may be termed 'multi-lateral regionalism', more in context with the lines of production of the various economies and the elasticities of demand

---

trade in the present Marshall area. (Economist, December 17th, 1949, Page 1340). In 1938, Western Europe imported foodstuffs worth \$1,685 million from East Europe.... In 1948 it was \$307 million (Economist, December 10th, 1949, Page 1276). It is readily seen that a whole question of the Pattern of Trade emerges as the most significant factor.

1. 'International trade in the 19th century functioned more or less smoothly because all countries had a high income elasticity of demand for imports.' (Economic Journal, No. 210-11). E.g. a 5% fall in the American national product caused a 30% fall in American imports. c.f. the statement "The general economic relationship between Europe, the dollar area and the sterling area, between manufacturing nations and primary producers, between competitive economies and complementary economies is most decidedly not solved, and it is to this wider problem that the attention of statesmen should begin to move." Economist, February 11th, 1950, Page 299.



of the respective importing countries. Briefly, the point is this. The agricultural countries need capital equipment and precision goods of various sorts, nor can they wait for delivery dates of the type with which they have been so far confronted by the older industrialised countries. In the circumstances they must launch on vast import programmes from the U.S.A. Meanwhile, the older industrial countries are feverishly producing in maximum quantities, for settling of their indebtedness with the United States by direct exports to that country.

These goods (a) at the given prices encountered sales resistance for which the failure of effective demand in the United States could not therefore be adduced as the reason and (b) in any case would be slow to sell in the highly industrialised American economy. It is clear, on the other hand, that the same quantity of output could be absorbed by the vast agricultural countries awaiting development. The result is that the U.S. economy is being invited to make a double volume of exports—Viability Aid to West Europe and Development Aid to Agricultural countries—when the second of the two should be undertaken vigorously by Western Europe, with the exports of the agricultural countries to the United States meeting all or (realistically speaking) most of the export-import gap of Western Europe in regard to the U.S.A. The point is not that Western European exports to the U.S. must or need cease entirely—far from it—but that the limiting point in their exports to the United States is reached in relation to their imports far too soon and that the means of meeting the balance is fairly abundantly present in the exports of the agricultural countries so long as the latter are not driven to incur large import programmes from the United States itself.<sup>1</sup>

If a system on the above lines were in operation today one unsettling result may, however, be noticed. The American economy whose rate of capital creation seems to be excessive today

---

1. c.f. American Economic Review, September 1948, Page 522, Haberler points to a fallacy in the E. C. E. Report which, in discussing the potentialities of European expansion argues against the possibility of achieving an export surplus with countries outside the U. S. (say South America and South East Asia) and using this for settling the trade deficit with the U. S., as something "extra-ordinarily unpromising because of the serious deterioration in the trade balance of non-European countries with the U.S." The reason of that deterioration, objects Haberler, "is precisely the fact that those countries have to buy in the U. S. all



will need to launch vast capital export programmes in order to relieve the internal economy of the accumulating pressure. Suffocation in this field involving unbalancing of the U.S. economy and a depressional collapse there, is as disruptive to the world economy and to the agricultural countries as is a chronic debt-ridden Europe. To that, however, there can probably be only one answer. While a country is faced with a strictly defined category of goods (as the exports of West Europe are) it has a claim to be exempt from the charge of a failure of effective demand within its economy.

In a background, however, of the combined exports of West Europe and the agricultural countries the argument loses almost its entire force and the correct way out must be acknowledged. This would mean two lines of action, both based on the assumption of U.S. responsibility for its net surpluses (i.e. over whatever Western Europe and the other countries can or need to import). Granting bold direction in economic policy there is no reason to feel that the wants of the American consumer (in real terms) can have been all met—there should in fact be no limit to the variety of facilities and conveniences of life and activity that a country with the means can provide. The provision of adequate consumption goods of all grades ranging from the essential nourishment for life to the facilities of travel and communication and so on, are all vistas on which the surpluses could be expended. The second point, which is related, is the raising of effective demand (through wage levels, social insurance and so on) within the economy. Both lines of action may be said to add to effective demand, the

---

those manufactured goods which they used to get in Europe. If Europe were again able to deliver these goods and to dislodge U. S. exports in Latin America etc. those countries would automatically develop an export surplus with the U.S. which could then be applied to Europe's trade debit balance with the U. S.

"Of course, there may be all sorts of difficulties and obstacles; Europe may have to make price concessions to recapture its markets in Latin America and elsewhere, but the chances are certainly not bad. Those countries are used to European goods and the German example after the last war proves that in a short time the old trade channels can be re-opened..." c.f. Dr. Schacht 'Gold for Europe' page 119 "...in 1930, I urged that foreign credits should not be given to Germany but to industrially undeveloped countries, so as to enable them to buy capital goods in Germany and other countries...." He ties up the Marshall Plan with Point Four and says "What is important is the question of what the European countries can in their turn contribute towards the planning and preparatory work.... I am afraid that it appears that European economists have not realised as yet the extraordinary possibilities of Point Four. It looks indeed as though they were still clinging to their traditional views on commercial and colonial politics."



one extensively and the other intensively. In practical application, the policy is not as easily done as said, but it would not condone the non-application in practice of sound economic policy in a situation such as the above. It may also be added that no exchange manipulations or tariff reductions could be taken as being basically a substitute for this primary obligation. Besides, it is well to remember that a raising of effective demand within the U.S. in the fashion noted above will in all probability increase the demand for imports and provide thereby a substantial improvement in the set up for healthy international trade. In regard then to the U.S. paradox of 'poverty' plus foreign surpluses, one may say that the economic structure must be readjusted to leave, in the export sector, capacity only for such output as, with the maximum import programme (including tourism), will over a period of time just balance payments. We say 'over a period' because in this is included temporary surpluses of capital loans etc., which it is known can and will be repaid by other countries and be absorbed by the U.S. The rest of internal capacity can well be devoted to rid the economy of the paradox.

## ( iv )

Yet, if we project the present circumstances and trends into the future, there does not appear to be much chance of the emergence of the trade pattern referred to above. At a time when the state of the Western European economy and the Sterling Area is parlous, any further disruption within these groups, however advantageous to a section or sections therein, is bound so much to endanger economic stability that any third trade pattern will have to be carefully considered. Countries participating in that pattern will have to give due allowance to repercussions on their own levels of activity and employment, of any breakdown in West European economic levels. And yet that does not mean, for instance, that a theory of salvation for the agricultural countries of the Sterling Area, as being contained in their being attached to that Area, is essentially true.

As a long run proposition the opposite in fact is probably true. It is interesting to examine, however briefly, the nature of such a third trade pattern and the implications of that for the agricultural countries in terms of their balances of trade and employment level.



The first point to note then may be that certain significant adverse changes in the trade pattern of South-East Asian countries since 1939 are really temporary. It will be noted that the pre-war supplies of rice to the South-East Asian countries came from these countries themselves. It is expected that even the imports of wheat into India should decrease very considerably in a few years. Viewed in this context, the adverse balance of India in recent years, especially in dollars, will accordingly become a favourable one in a sizeable period of time. All the evidence indicates that the responsibility for the fundamental economic change after 1939 lies really in this vital disturbance of one of the most prominent features of pre-war intra-Asian trade. Assuming then that what we call the normal pattern is restored, we could say that in respect of current trade the problem of convertibility does not arise at all. On the contrary, a fund of exchange resources will be available for considerable capital investment programmes. The size of such resources is, however, bound to be somewhat limited by certain well-known facts. The dependence of these countries for simple consumption goods on imports is enormous and as such not much of the foreign earnings would be left for capital import programmes.

The following table<sup>1</sup> although it includes all imports, that is from Asian countries too, gives some idea of this dependence.

Average for 1937, 1938 and 1939; Values—Millions U.S.\$

Countries	Rice	Sugar	Textiles	Textile Making Machinery	Total of 2—5	Total Imports	6 as % of 7
India	44.1	4.4	72.9	39.8	161.2	550.1	29.3
Burma	—	.5	20.3	—	20.8	77.6	26.8
Ceylon	19.4	2.5	9.9	—	31.8	89.1	35.7
China (excluding Manchuria)	15.3	9.0	17.2	20.3	61.8	315.0	19.6
Manchuria	3.5	9.0	49.2	7.8	69.5	329.9	21.0
British Malaya	31.4	5.8	21.4	—	58.6	258.8	22.6
Netherland E. Indies	9.4	—	62.4	—	71.8	250.0	28.7
Siam	—	1.5	11.8	—	13.3	51.9	25.6
Japan (proper)	0.9	2.3	3.0	226.9	235.1	867.3	27.1
Chosen	2.0	3.0	56.0	7.2	68.2	329.8	20.7
Taiwan	—	0.3	0.8	7.4	8.5	88.8	9.6
Iraq	—	3.0	10.0	—	13.0	44.0	29.1
Persia	—	6.0	14.0	—	20.0	60.0	33.3
French Indo- China	—	—	12.6	3.9	16.5	59.7	27.6

1. Ghate: Asia's Trade, Page 81.



The percentages for Burma and Siam, which produce large amounts of rice, and for India, which manufactures textiles, probably bring out the position in greater relief. On the other hand, 45% of Asian imports are from Asian countries and 42% of exports to them. It is probably not wrong to take that as an indication of the degree of complementarity existing in the various types of products within this region. The following tables would help to verify the position further.<sup>1</sup>

### Share of Metropolitan Powers in Pre-war Trade of A.F.E. Countries

Imports			Exports		
1928	1935	1938	1928	1935	1938
30.9%	28.1%	30.5%	21.4%	28.0%	31.1%

Korea's Trade—Japan's Share	
Imports	Exports
1935	1938
84.7%	87.3%
88.2%	80.8%

The position of this region appears to be more suited for joint endeavour than some other agricultural Regions, as the following estimate for Eastern and South-Eastern Europe seems to indicate, where imports from outside seem to dominate the trade position.

### Estimated Annual Demand for Imports at Rising Income Levels<sup>2, 3</sup>

S. E. Europe	National Income £million	Total Imports £million	Imports from outside the region £million
Before expansion	1,400	170	152
After expansion	2,135	235	210

1. Report of Ecafe (1949) Page 209.

2. Mandelbaum, Page 89.

3. Eastern Economist, November 26th, 1948, Page 923—The Industrial Working Party, recognising this point, recommends the establishment of a Committee for Industrial Development to arrange interchange of raw materials and finished products, and to make recommendations for pooling of orders and for standardising equipment for transport and agriculture. This Party and the Agricultural Requirements Working Party have both urged that the Japanese capacity for supplying capital goods should be tapped. This is possible if the Ecafe countries relieve Japan of her dependence for imports of food and raw materials on the U. S. A.



That a state of development and full employment will further raise the volume of this intra-Asian trade by a vast amount is beyond doubt. There is the historically observed truth that, in all countries, increasing industrialisation has led to generally increasing imports; there is also the vast reservoir of hitherto ineffective demand of one fourth of the earth's humanity; and there is the fact of general trends towards overproduction in raw materials which would now find the solution which was unavailable to them all these recent decades. "The industrialising countries will trade more intensively with each other as their productive capacity develops, and this exchange between them will increase relative to their trade with the mature areas." "This follows from the broad rule that the degree of complementarity between industrial countries is higher than between primary producing countries, but lower than between primary producing and manufacturing areas."<sup>1</sup>

The percentage share of intra-Asian trade need not necessarily go up; it will probably not for some time, since the previous imports of simple manufactures from outside the Region would have been replaced by imports of precision goods and so on, and because of vast programmes of capital importation that will necessarily be required. In any case, the facts are clear. The development of every agricultural country will provide the basis for increasing development of natural resources and for increasing intra-regional trade, and the latter in turn will help standards and development in every individual country. The special significance of this in our context is based on two observations. One, the trade of every country among these could be automatically balanced within the multilateral net-work of that Region (or by setting off some of the external earnings, the drafts on which, however, are for this purpose not at any time likely to be considerable.) The second basis is the almost universal surplus of foreign (and especially dollar) earnings to this Region on current account. This follows especially as a consequence of strong natural factors, and on the general principle associated with increasing intra-regional development.<sup>2</sup>

1. Mandelbaum, Page 17, affirming A. J. Brown, 'Industrialisation and Trade.'  
2. c.f. e.g. The following table:

	Sterling Area Exports to the \$ Area (£ million)			
Primary Products:	1938	1946	1947	1948
Rubber	16	34	57	45
Jute	6	22	21	43



Such an Area then, of which the geographical extremities could probably be the Rupee and the Yen, holds every promise of operating with success—and that means becoming a strong currency Area, as well as becoming a great support to the economic development programmes of the countries of this Region. It is yet true that full employment will be indivisible. A fall off in demand in the United States can directly, and a collapse in Europe indirectly, certainly jeopardise the stability of this Region. Yet, the increase in vigour intra-regionally in respect of trade and production is bound to afford much cushioning effect to these countries in the event of extra-regional fluctuations occurring at any time. Besides, this same vigour is bound to impart strength to the productive effort of the extra-regional countries of the world and then in turn back to the region too. It is needless to expand on this truism which may tend to descend to mere quibbling. The whole global system may be considered a moving equilibrium (in the best traditions of fundamental equilibrium analysis) and any change at any one point may be taken definitely to have its repercussions throughout the entire system before the latter moves into a new equilibrium position whether at a lower level or higher. A recession anywhere will certainly tend to drive the system to equilibrium at the lower levels. But strength anywhere is bound to be a contribution towards equilibrium at a higher level. Whether the full effects of this contribution will be realised is another question. It is at this point that the mechanical position earlier referred to, of Western Europe failing to organise vigorous capital export programmes to agricultural countries, assumes relevance. If the agricultural countries balance their payments directly with the United States, Western Europe probably only increases the nature of its own tasks; if the agricultural countries balance indirectly, by importing (not consumption goods but capital equipment) from Western Europe, the task of all going happily forward together is probably made far more easy and realisable. In either case, the agricultural countries benefit by a Regional scheme—though in the latter the United

Wool	...	2	37	39	34
Cocoa	...	1	10	20	27
Tin	...	6	—	8	20
Tea	...	2	11	12	14
Diamonds	...	—	9	4	5
British Manufactures:—	...	24	44	58	96

These figures do not show the surplus or deficits but they indicate that Primary Products add up to a far greater contribution than the manufactures.



States will have to assume sooner its responsibility of curing insufficient internal demand. It may also be repeated finally that the fault, in case of non-adoption of the latter, is however not with the agricultural countries today.

It need hardly be said at this stage, save for the sake of mere reminding, that the system of buffer stocks (and its appurtenances) which as we have earlier seen, is only of secondary significance in aiding the achievement of full employment, is as an aid to stability in international trade, equally only of secondary importance.<sup>1</sup> The risks sometimes of relying on a buffer stock system are already known. But the more significant factor seems to be that in the present states of production in the various economic regions of the world, a stagnant and low level of demand in a major section of it must necessarily block the realisation of the basis of true international stability which is a reintroduction of global balance in trade, and balance at a high level. The balancing at a high level is necessary both in itself and because conditions of expanding trade volume are far more easy for the striking of balance by all countries both surplus and deficit. Stable, and especially falling levels may create further rigidities and deficits.

(v)

To summarise:—traditional trade cycle theory, with its illustration of commodity and capital movements between countries, and the foregoing examination of certain more macrocosmic influences, together make more than clear the point about the intimate relation between World economy and Internal full employment. More important than that is to give full cognizance to the complexities in range of the several possible patterns of international economic organisation that can exist, and the difficulties as well as the absolute necessity to make the correct decisions in choice. In the absence of the desiderata mentioned above, neither buffer stocks nor internal full employment can stabilize the position for the agricultural countries.

---

1. The same must be said of Stabilisation Schemes, a system of 'cash buffers' tried out in the Gold Coast and Nigeria in so far as achievement of full employment is aimed at thereby. c.f. *Economic Journal*, December, 1952, Bauer and Paish pp. 750 et seq.



It is certainly true that goods produced for home and intra-regional consumption will not be directly affected and that these will form the bulk of national wealth. It is also true that after development a much more advanced system of social insurance and services would begin to function and large resources from trade during prosperity could be saved up (as is being done in New Zealand, for instance) for disbursement during depression. It is true, therefore, to say that the development policies in agricultural countries will without doubt secure much the greater part of the standard of living and the solvency of the agricultural countries. As we said in an earlier chapter, however, agricultural exports though now dethroned from their reigning importance must not be considered entirely negligible in the scheme of things and the capacity to influence that scheme. The effect on the agricultural exports caused by external depression, coupled with consequences of the latter for capital and allied imports is bound to cause considerable fluctuations in income.

It is as much in the interests of the agricultural countries later on therefore, to make every contribution towards world economic stability, as it is now for the surplus countries to help in the resuscitation of the deficit and depressed countries. In the long run, the responsibility for full employment, as much as full employment itself, is indivisible.



## CHAPTER FOURTEEN

### Re-instatement of General Theory

LET it be said immediately that by General Theory we do not necessarily mean the original Keynesian framework outlining the set of forces responsible for a given level of employment in an economy and the devices consequently recommended for stability, especially as expounded in their orthodox form. We, however, would not only admit but emphasize henceforth the applicability of General Theory to agricultural countries; and its necessity for the final emergence and stabilising of full employment. Whatever the additions necessary to the accepted armoury of 'full employment devices' under the Theory, that these devices will come into their own henceforth needs to be strongly recognised for more than one reason. It is useful then to talk of a General Theory—the broad lines of which are certainly accepted almost universally—into which the observations below could be worked.

(i)

At the beginning of this thesis, the point was made that besides severe unemployment there has always been chronic and depressing under-employment. In the course of our study later it was further concluded that in the process of tackling the problem, the objective would be 'standard of living for all' rather than 'employment for all' and that the Development programme would be framed and operated in that context. Theoretically, the programme in organising all resources under a plan, effecting optimal combinations and eliminating surpluses at every stage, should produce two beneficial results. It should exorcise the previous type of under-and unemployment, which we will now refer to as 'endemic unemployment' and it should also produce the maximum standard of living under the circumstances existing. In actual operation, however, two points need to be noted which, jointly, will leave a residue of unemployment in the economy. The rationalisation of the economy in terms of the standard of living will be labour-intensive in comparison to advanced countries. But it will not be 'intensified' to the point of employing more labour than what the given capital equipment requires. In the present state of capital starvation in



agricultural countries the consequences of such organisation will be some 'residual' unemployment in the population. The other point to be noted in practical operation is the fact that any level of employment is contingent partly on completely satisfactory mobility of labour, using the term in a broad sense to include inertia and the other factors like training etc. This is a well known and accepted point and the term 'frictional unemployment' used in this context refers to a technically unavoidable minimum existing in the unalterable 'make-up' of human nature, faculties and organisation. Now both these types of unemployment must be expected in the agricultural country after development. It has been customary, granted efficient social services, to recognise effective full employment as achieved in an economy despite the presence of the minimal 'frictional' unemployment referred to. But the former type arising from the process of rationalisation and which we termed 'residual unemployment' is, whether in the presence of social services or their absence, certainly not appropriate to a level of full employment. It is not frictional by any means and can be considered unavoidable only in the abstract state of no more amenities, facilities and public works being required for the population or of no natural resources existing for such work. That this state is highly conjectural was mentioned earlier and with a purpose. The well-nigh immeasurable need for various things like houses, roads, recreational facilities, entertainment and education entail a volume of demand for labour in the midst of which a state of 'residual employment' would only constitute one more to the several paradoxes weighing down the dismal science. Full employment can be said to be secured only when the useful additions to national wealth that this residual labour power can make are made. There is no doubt then that the absorption of this surplus labour in the country should be effected in every reasonable manner. It will be noted that, with the diversified and sufficiently integrated structure in the economy, the effects of such employment are bound to multiply internal prosperity and not to damage either the balance of payments situation or the economy behind it. Supplementing these 'public investment' and 'public works' programmes, will be the 'feeders' of purchasing power like 'Beveridge', both to meet the situation caused by frictional unemployment (in which one may include old-age, maternity etc.,) and generally to strengthen purchasing power within the economy.



There is next, the third most significant type of unemployment that will emerge. So far, that is till the economies came to a state of 'full employment', it would have been generally correct to say that the unemployment problem real would have been more 'endemic', and 'epidemic' unemployment only a superimposition (significantly troublesome though) caused by fluctuations in world economy. (In a country like Ceylon, for reasons earlier stated, these fluctuations affected most sectors of the economy. But it did not mean that unemployment was epidemic in the sense that it was the ruling feature; unfortunately it was worse—it was both). In the new state of development, the emphases will change radically. For one thing, endemic unemployment will cease to manifest itself and a new unemployment problem will emerge. It will be the traditional unemployment in depression characteristic of all industrial countries. Two things need mention in this connection. First, it will be an epidemic unemployment liable to show itself only at intervals and in the form of sharp mass unemployment. But, to repeat, it needs clearly to be distinguished from the epidemic unemployment to which agricultural countries had been hitherto used, namely those caused by depressions in prices of agricultural exports.

Also, the new epidemic unemployment will be induced by forces generated from within the economy and operating within it, in comparison with the other which is dictated by fluctuations in world markets. Secondly, the possibility of this epidemic unemployment is dependent on relatively uncontrolled or uninfluenced operation of internal economic forces. In practice, this unemployment may not occur and that is the major point of our theme here. With the integration and complementarity in the structure, the traditional devices for the maintenance of employment, as well as the feeders of purchasing power like 'Beveridge', will find themselves automatically reinstated. The maintenance of purchasing power for the avoidance of depression or the stimulation of activity as well as the directing or effecting of investments become all analysable in terms of modern employment theory. General Theory then not only assumes relevance by drawing in the residual and frictional unemployed into the scheme of things but will play its role in counteracting fluctuations and steadying the course of economic activity. In



the nature of the planning discussed in an earlier chapter, the dominant emphasis was on actual investment rather than inducing investment by disbursing purchasing power. There would need now to be a re-alignment of emphasis within the framework of the plan, and 'Beveridge' and public works will begin to play increasing parts. The safe-guarding of the development achieved and especially the stability of employment at the new level will, therefore, make imperative the introduction of the traditional full employment devices. The economics of full employment in agricultural countries will tend to fall more in line with the economics of full employment as theoretically expounded in and for the advanced economies. To all intents and purposes, the reinstatement of General Theory will have taken place.

(ii)

To revert to the opening statement of this chapter however, it is necessary now to ask whether the reinstatement of general theory is entirely true. The contributions of its weapons to the maintenance of stability cannot be denied. The question is whether they are not really insufficient, and whether it is not necessary, within the orbit of the general theory or without, to recognise certain other vital weapons as well of policy. In the first instance, as we noted earlier, the general theory in assuming the ample flow of capital supply assigned to consumption an ability to steady employment levels which does not seem to be completely borne out by experience. It would be wrong to infer that the Theory needs anything more than an alteration of emphasis in regard to the various functions it embodies. For it is true that the problems relating to the efficiency of capital were adequately recognised within the framework of the Theory (though, in its practical bias, it was not expected to present a problem at all); and that, therefore, even a major shift of emphasis in regard to the policy for full employment can really be worked within the framework of this theory. Yet, the distinction must be clearly made and remembered.

With the slowness of leaf-raking, even in the U.S.A., in retrieving situations completely, a new emphasis must needs be assigned within the framework of the theory to the investment and direction of capital. In our context, it will mean a continuation of the planning



earlier outlined, though it may be in a modified form. It is on record that the author of the General Theory expressed the opinion in conversation in the U. S. A. just before his death, that the idea originated by him of the euthanasia of the rentier has been carried too far.<sup>1</sup> If so, it is clear that at the reinstatement of general theory in agricultural countries, the full employment devices must still include, whether through the Planning Authority or otherwise, the 'rentier' functions and cannot depend on the strengthening of consumption alone.

The necessity for such action is further reinforced by the dynamic forces entering into a determination of employment level and to which we have already referred in Part I of this Book. The validity of that theory of dynamic economics would give us again the conclusion that at any time the problem of full employment has to be tackled at least as much from the investment end as from the consumption end. It means the same care must be devoted to observation of both ends, though at a given time policy proper may have to be weighted at one time in terms of purchasing power and at another of investment. On the assumption that at an existing rate of accumulation of capital stock consumption cannot exceed a certain level unless investment is stepped up, the conclusions for policy follow naturally. This aspect of policy can fit into the General armoury for full employment—though beyond a point, and especially on our presumptions about Planning, the final version of the General Theory may not be recognised by its orthodox Elder! For one thing, the collection of data will be equally in dynamic terms, and not in semi-static alone. The trends of population, of capital stock tomorrow in relation to the daily additions to it, and in relation to consumption tomorrow, and the decision thereby either to reduce or step up rate of capital creation, and so on—these problems will take equal place with the other data arrived at by study of inventories, unemployment figures and so forth.

It must be said that these points have been raised as they have some connection to the subject of the Thesis but that it is not hoped to assess them completely in any sense. The more important part of our study has been the actual economics of agricultural economies as they are today; it may be termed an economics of transition.

---

1. American Economic Review, May, 1948, Page 287.



Any adequate study of the above points would constitute a separate volume in itself and from the point of view cannot naturally fit in here.

(iii)

Together with the foregoing remarks on General Theory it may not be out of place to observe briefly on the counterpart of general theory in the sphere of international relations. The evolution of international currency based on stable internal wage levels and flexible exchanges operating in a multi-lateral setting is in fact part of the Keynesian revolution. The partial irrelevance of some aspects of it and the inadequacy of others, we saw in the previous chapter. In the post transitional stage, however, (when that will be is another point) if we could assume general high levels of employment throughout the world and the basis for long term balance in the payments of the countries entering into international trade, the present framework for International Currency should also find itself suited in its essentials to the various economies, both industrial and agricultural. It should in fact be a desirable instrument of action for the agricultural countries. For, with their new complexity and variety in the structure of production, both input items and output will be correspondingly diverse. The influence of that in international trade will be reflected in an increased complexity in their import items and (at least intra-regionally) a correspondingly marked variety in their exports. A simple exchange, only a little removed from bulk purchase or sale-cum-bi or tri-lateral circuit, would probably be less possible and also less advantageous; with the result that the tendency would be nearer to the ideal multilateral trading, arriving at global balance. If that be the setting, International currency would fit in perfectly into the new economic system. Whether that setting for World Trade Organisation will emerge tomorrow depends on the decisions taken today.

A word may also be said about buffer stocks in the event of the new validation of general Theory. Briefly, the purpose of buffer stocks being to deal with a situation caused by forces from outside the economy, their value cannot be considered diminished in the new context. But for the same reason, they cannot be considered in any way relevant to the maintenance of stability in the internal



economic system as such; although to the extent that they aid certain industries therein they facilitate the task for the full employment devices of keeping the economy in control. It must be repeated, however, that even in its own field the buffer stock system is valid only to the extent warranted by past experience; and therefore the urgency for stability by other means becomes even more necessary.

Broadly, we may conclude by stating that this new stage we have been referring to in this chapter would be the appropriate place to pursue a vigorous policy of public works and services in the widest sense, but that in view of other considerations raised here, it would be wrong and dangerous to forget the continuous reality of an investment problem in the midst of an over enthusiastic devotion to consumption. In fact, policy cannot any more assume the dynamics of the economy to be broadly such and such, but must be devised increasingly in the light of data derived from a dynamic study of the forces operating with a resulting emphasis now on investment devices, now on consumption devices and a third time probably on both.



## CHAPTER FIFTEEN

### Summary and Epilogue

A summary does not summarize without at the same time divesting itself of much of the context in which the content of the original has been placed. So, while what is stated here is not a mere card index to the various chapters preceding, it should not at the same time be considered to be either comprehensive or even completely explanatory.

The economics of full employment we found was not something that could have general application, if by that was understood the deductions from the generally accepted theory of full employment. We also found that the theory was being sternly urged as inadequate even on its own ground in view of the virtual neglect of the dynamics of economic activity. To that extent the economics of full employment in agricultural countries too would have to be as different from 'the accepted' notions as in the industrial countries; indeed, it seemed very likely that, on the postulate of the economics of agricultural countries being coincident with the economics of development, the fundamental concepts of dynamic economics would enter more prominently and more persistently than in the advanced countries. But the more urgent and deciding concepts in our investigation were those relating to a demonstration of the strong inadequacy of the 'accepted theory' when applied on its own assumptions itself.

From that angle chiefly, though not entirely, we attempted both an adjustment of the theoretical foundations and an examination of the practical set-up and so on necessary in transferring the theory to the field of real activity. This examination we sought to do in general terms and in relation to concrete cases (India and Ceylon), confining the former chiefly to the earlier and the latter to the subsequent portions of the investigation. Such examination perforce covered a broad range of subjects, as the case for development, the nature of diversification of production and of integration required, the degrees of State participation in actual activity, the economic system in detail of the two countries chosen as concrete instances, the structural framework called for in the case of these concrete



instances, certain vital questions like those of high cost industries, of protection and of social welfare, the nature and degree of planning, world stability and interrelation of economic prosperity internationally as well as the possible courses of action for agricultural countries severally or jointly in the international sphere, and finally, the emergence of a meeting place for the various present discordant tools of full employment policy, a context in which buffer stocks as much as Beveridge and a General Theory as much as Dynamic theory would not only be 'non-conflicting' but also mutually helpful. In the result, it is hoped, a consistent line of argument has been produced which should provide the starting point for development activity in agricultural countries and detailed theoretical investigations on the several aspects of that activity.

In building up our thesis on the foregoing lines we have begun with the point that the need for a special study of the subject arises from the fact that besides severe unemployment there has always been chronic and depressing under-employment in most agricultural countries; and, coupled with it, the fact that the theory of full employment has been inferred from, and is applicable mainly to, economies with diversified and well integrated structures of production. (Chapter 1.)

A definition of the term 'agricultural countries' has been attempted as necessary to a proper pursuit of the investigation. It was pointed out that the key to the sense in which the term is employed was the undiversified nature of the economy, in the sense of a lack of certain wage goods industries, especially in a general state of under-development of the economy as a whole. (Chapter 2.)

We have followed up (a) with a review of certain general but salient features in the economics of agriculture per se, in view of its essential relevance in formulating any industrial and employment policy in these countries; and (b) with an examination of the economics of agricultural countries. Among the subjects considered under (a) were the nature of the Supply function, the nature of demand, location, size, marketing, earning capacity of agriculture, the several types of fluctuations in agriculture, and State interference. Under (b) were considered the structural set-up and the implication in terms of the balance of payments, incomes, employment, stability, bargaining power, social welfare policy and the futility of 'full employment' devices. (Chapter 3.)



These preliminary aspects of the Study led to and were rounded off by a critical resume of the theory of full employment as developed and accepted in and for industrial countries, and a statement of the nature and extent of its irrelevance—and relevance—in agricultural countries. The theory and its technique were not disputed in their broad outlines. The devices commonly associated with it were however found unacceptable. Too much emphasis was paid to the 'inducement to consumption' aspect and too little to the 'inducement to investment' aspect. To us the latter was seen to be the crucial feature; the former was to come in only through increasing wages bills for the new 'industries.' (Chapter 4.)

*Part Two* of the Study is prefaced by an examination of the term 'full employment' wherein the alternatives have been posed in the form of 'employment for all' or 'standard of living for all' with an awareness of the fact that one need not necessarily mean or entail the other and that therefore they may be contradictory instead of being complementary. It was observed that a Development program with standard of living as the target would be broadly the recommended policy as well as the interpretation given to the term Full Employment in our Title. (Chapter 5.)

By inference from the foregoing conclusions, by collation of other general principles, and by substantiation with data, the case for a Development program in agricultural countries has been then rationalised and the ground made sure for the particular type of full employment policy advocated in the Book. (Chapter 6.)

The task of development and increase of production, however, could not be left at that since as much depended on the type of development as on the development itself. On the question of mere indiscriminate increase of production, the conclusion obviously was that diversification is necessary if the deleterious effects of the lack of an integrated structure and of disadvantageous terms of trade etc., are to be avoided. The crucial question was, of what sort the diversification should be. Was it to be (a) of export industries or (b) a new set-up of industries producing goods that would replace imports or (c) of other industries like house building, furniture making etc. The balance struck was based on (b) above with a certain proportion of (c) and wherever feasible under world



competitive conditions of (a). In the course of these deductions the meaning of the term industrialisation also came up for clarification. Whether industrialisation means higher incomes necessarily and whether it excludes agriculture, were important questions. Application of the principle of optimal combination of factors gave various optima in respect of the degree of capital intensity for various economies (and regions) in relation to the intensity of the presence of the several factors concerned, viz, resources, labour, capital and skill (managerial and technical). Just as much as a degree of organisation below these optima represented lower incomes, equally certainly a degree of industrialisation that exceeded these optima could not bring higher incomes. Large scale programmes for agriculture, raw materials and certain 'processed' consumption goods would all come within the term industrialisation. (Chapter 7.)

For such an ordered scheme of economic development, it was natural to infer that the 'consciousness' represented in the individual firms and units was not enough and that a more comprehensive, even a Unitary 'Mind', may have to intervene to formulate policy and direct programmes. Thus the question of State participation in development policy arose. Would it be the provision of certain basic needs like hydro-electricity, railways etc., hoping for the rest to come by itself; or would it be a Russian (by which is not meant 'communist') plan; or a 'Bombay' plan? In short the question was, between complete planning and complete laissez-faire at what point would we rest and find the ideal basis for development of the backward economy. It was generally concluded that not planning through deficit spending (however accompanied by other controls and directives) but planning through Investment Boards, is what is required. The 'institutional framework' must treat the economy in the nature of a 'huge firm or trust'; but the mechanism of finance need not be all State. An incorporation of public finance through a series of Public Corporations at every possible stage is the desideratum—together with the giving of free room in sectors wherever private hands are expected to be willing and able to undertake responsibility. Foreign borrowing, which should be tied to the import of technical skill and the capital goods proper, is, all things considered, better done at Governmental levels and in any case has to be regulated and controlled by the State. (Chapter 8.)



In developing the analysis further we sought to do so by selection of two concrete cases. At this stage, *Part Three*, an examination of the structural set-up in India and Ceylon has been made. These included analysis of the concept of under-employment and a review of further production possibilities in tea, rubber and so on. Among the other aspects studied were the intermediaries between agricultural produce and the final market, the vicious circles in several spheres of economic activity, the absence of efficient monetary mechanisms, the virtual absence of self correctives and the helplessness (made worse by population pressure and at least a century old lag in development) in the consequent state of low level equilibrium. This study served to bring out in full measure the facts of agricultural economies of which we had so far talked in theory. It was concluded that the economic structures were in many ways out of joint. (Chapter 9.)

From there we moved on to the formulation of a full employment policy, in which the first task was the working out of a correct structural framework. Certain vital background features to be desired were discussed, and a framework worked out subsequently. Among the subjects considered and given their due place are: the items of agriculture and of industries considered basic and necessary, the secondary industries entailed, decisions on size of various units or lines of production, location, the vital tertiary industries, their organisation and the method of their linking with primary groups, training and skill, an appropriate and efficient Finance and credit Structure and the various new attributes and alterations called for, the role and rationalisation of the plantation industries, the further export industries possible and feasible, and the industries that are neither export nor import substituting (i.e. 'domestic'). Broadly, the following framework may be said to represent the position; (1) wage-goods industries are the basic industries; (2) full employment by development (rationalisation and investment) and not by any adjustment within the existing framework; (3) both farm and factory must come in and at a relatively high level of co-ordination between them; the pattern will be one equally of small or 'cottage' and large-scale units. Development must cover Wage-goods industries, feasible export industries and ancillary industries in the tertiary sector as well as feasible small-scale machine manufactures required in the agricultural and industrial units contemplated; (4) the process shall be



by eliminating 'surpluses' at every stage and going on creating optimal combinations all along the line (and not by being satisfied with sluggish activity like 'public works') till final full employment is thereby made possible; (5) Institutions required will include those for Planning, Direct Finance of Industry, Technical Assessments, and Research. (Chapter 10).

Next, some vital problems which force themselves in the formulation of full employment policy have been considered. Certain essential industries started may have to run at a loss. Is it economically sound? What policy of protection is it best to adopt to preserve these industries in the economy? What is the relation of these to social insurance, unemployment allowance and public works policies? The economic feasibility of certain industries run at a margin of loss, the soundness of protection and especially of subsidies in our economic context and the intimate relation of the latter to social 'insurance' is demonstrated. As for social security itself, it was concluded that it could well be considered simultaneously in point of time, but not in point of importance. The scheme should be carried as far as but only as far as the larger purposes of economic policy would permit, and introduced also in a manner such as these larger purposes will allow. To that extent, no better start could be contemplated for an advance on the social welfare front than a welding of subsidies into an industrial policy. (Chapter 11).

The third and final aspect in the formulation of full employment policy has been the subject of planning. The case for it has been put forward, and an outline of the planning procedure and assessment of costs attempted. In the course of this attempt, the unreality of much that goes under the name now is emphasised, the distinction is made between plan and programme, the need for complete co-operation of all elements in economic activity is brought out, the importance of ensuring consumption is discussed and the question of wages is briefly answered. Finally some concrete instances of 'Plans' have been taken up in illustration of some aspects, especially the working out of total costs. The Colombo Plan, chiefly in relation to Ceylon, has also been critically reviewed. The broad conclusion is that Planning of a fairly comprehensive type is certainly necessary if we are to utilize the



lessons of our conclusions from the previous chapters, but at the same time it is neither authoritarian planning nor loose collation of Departmental proposals. (Chapter 12).

In the next chapter, *Part Four*, we have left the somewhat 'sealed' atmosphere in which internal full employment has been worked out, to observe the international economic position today and to postulate the conditions necessary on the one hand and what the agricultural countries should or could do on the other. The present external discrepancies reflected in international trade militate decisively against both stability and full employment in agricultural countries, and the existing international agencies, while useful, are clearly insufficient to solve the problem. The present organisation of world trade patterns is felt to be harmful both to the surplus countries and to the deficit countries of West Europe. The scope for expanding Intra-Regional trade, for example in South-East Asia, is demonstrated and it is suggested that while its import problems can be solved by a trade link with America, it would really not solve West Europe's problem—a point for which West Europe must really take the blame. For West Europe should have organised a vigorous capital export programme to the agricultural countries, with the global balance being struck by the dollar deficits of the former being met by the dollar credits of the latter—the obligation of the U.S.A. in that event to raise internal effective demand being accepted and implemented. The present food deficits of some of the agricultural countries vis-a-vis the dollar (not vis-a-vis the South-East Asian Region) are clearly felt to be temporary and the calculations about the best trade patterns for the future must look over and beyond this disappearing mist. (Chapter 13.)

The argument of the Thesis is rounded off by reference to a final stage in which the emergence of a meeting place for the various present discordant tools of full employment policy will be noticed—a context in which buffer stocks as much as 'Beveridge' and a General Theory as much as Dynamic Theory would become mutually consistent. Broadly, the conclusion is that this stage would be the appropriate place to pursue a vigorous policy of public works and services in the widest sense, but that in view of other considerations mentioned on the inadequacy of current 'full



employment' theory even in its own setting, it would be wrong and dangerous first, to forget the continuous reality of an investment problem in the midst of an over enthusiastic devotion to consumption and secondly, to assume any more for purposes of policy that the dynamics of the economy is broadly fixed. Policy should continue its touch on the pulse of investment and should besides base action more and more in the light of data derived from a dynamic study of the forces relevant, with a resulting emphasis now on investment devices, now on consumption devices, and often probably on both. (Chapter 14.)

If we must sum up in a line the economics of full employment for agricultural countries as we have developed it, it is a Policy operating through Investment Boards aiming at a goal of diversified production broadly in terms of 'wage-goods' industries and founded on the planned use of resources and programming of priorities for them. The reliance on mere full employment devices by State action and the committing of the rest to 'free forces' is comparable only to a staggered start in which the runners finally have equal chances. Ours, on the contrary, is a start with a handicap of centuries and hurdles much less customary in the 'rules of the game'. The absence of that hectic economic expansion of the 19th century in which every rising industrial country invariably found itself crested on a seller's market (for that would be a fair interpretation of economic imperialism) makes it more than ordinarily difficult to establish a case for industrialisation of the present agricultural countries on the basis of the 'accepted full employment devices' alone. Cases of Centrally inspired development as in Russia and the case of the T.V.A. in U.S.A. provide useful illustrations.

\* \* \*

We are now at the end of our enquiry. It may be interesting to ask whether the overall picture in the near future will really be as theory would expect. It is easy to see, of course, that nothing that has been said in the preceding pages is, economically speaking, incapable of adoption; nor is there any necessity, once the policy has been accepted, to doubt the capacity of present governments to carry it out. On our argument, the adoption of these should produce a picture of well diversified and fairly integrated structures producing a multiple of their present national incomes and balancing their payments with each other at a much higher level than



today. In actual fact, however, it seems doubtful whether it will turn out all just that way. We must be prepared to expect a considerable difference in the actual development that will occur. When we say that, we do not refer to the fact that change as contemplated above is necessarily a time-consuming process and that the new set-up may not finally emerge till well over a generation has passed. We are referring to the difference in the course of the development itself. We have already referred to the economics advocated in this Book as the economics of transition. The question now is whether this economics of transition will have a full chance to operate and produce that final picture which, in the abstract will necessarily emerge. Some broad observations may, therefore be made on certain limiting and impeding factors.

We must, first of all, grant some given material limitations and undercurrents. "Lies, damn lies and statistics" is in some sense vaguely true. Calculations on the extent of resources available or possible stepping up of yield or the capacity to repay capital imports, can, even with the best of estimates, turn out somewhat mistaken. On the other hand, it seems fairly certain that any such variations as are possible here cannot possibly so alter situations as to prevent the emergence of an overall picture such as was theoretically envisaged. The present indebtedness of the industrial countries to the U.S.A. may, however, be a more serious point. Any calculations based on the assumption that these debts could be paid off may well prove to be wide off the mark. The shaking up given to the agricultural countries by a declaration of bankruptcy at any time by the industrial countries will then mean probably an infinite moratorium on any attempt at change of the structures or at the least a far longer period of transition.

There are also certain social considerations which need to be recognised. It is true that the undercurrents today are definitely towards more modernistic existence of the individual in society, with the break up of the joint and large families, the general spread of quick transport and the enlarging scope of education. Yet, in real life, there are vast seas of humanity in several of the agricultural countries which are practically untouched by these changes which in the West have been concomitant with the spread of industrialism.



The lingering social stratifications and ties are bound to be obstacles in the path of development. Caste, for instance, would hinder the extensive development of a cottage industry which from the point of view of the country's economy may need to spread beyond the group at present engaged in it. Permanent mobility of labour may become only a desired end and hinder drastically all ambitious agricultural and industrial programmes. All these may then reduce the preceding thesis in one stroke to the status of an edifice built in sand; and the economics of agricultural countries may reduce itself simply to a hundred per cent education drive, or a revolution non-violent or violent, according to the particular philosophies or aptitudes of the particular governments and peoples. These are not within our competence to evaluate. But two things may be remembered. One, the social intractability of the population may not be so bad as might appear at the initial view; the go-ahead economic policy itself is likely to break down these barriers with more irresistible logic than any academic spoon feedings by themselves or any philosophies of revolution. Two, in a state of rapidly rising populations and very low standards of living, the postponement of economic development till the victory of social 'enlightenment', is hardly the circumstance in which to convince the 'hungry sheep' on the virtues of modernity in social life for ultimate economic salvation. This is particularly the problem in a 'democratic' context.

Where the setting is 'authoritarian' most of such conundrums may for practical purposes be largely figments of the imagination! The economic truths will be the same, and hard; but individual 'enlightenment' need not be awaited, in the same manner, as the motors of economic activity. The only practical answer can be the drawing up of sensible priorities of the type we referred to in the course of our Study. The tussle in every poor country, represented in taxation away from investment for expenditure on social services, shows up the problem. Both investment and social services are highly desirable and necessary, but both prosper (beyond certain limited points) at the expense of the other. Yet, in the long run given the present state, the benefit of investment makes more social services possible than vice-versa. If our impression is correct that, with the assumed minimum progress in modernising the individual in society, the back-log of social intractability will not



markedly slow down the development process and will ultimately be broken down by the latter, then the structural changes we theoretically envisaged will be substantially repeated in practice.

More problematic than the foregoing limitations, however, are those which we may justly term political. We do not attempt here to evaluate the tendencies or decisions in political spheres; but we need at least to recite them as data for our purposes. A big proviso is made initially—peace is assumed. Now there are certain things like rice, fuel for tractors and so on which war had and would cut off to a country like Ceylon. To the extent that these past experiences influence economic policy as well, the diversion of economic resources to that end would slow down the pace somewhat. In regard to the more important of such items, however, we already saw that their development was, quite apart from social or political desirability, actually economically feasible and desirable, and thus no conflict would arise. A few exceptional cases may still exist but they would not be major constituents of total National Income and so will not affect the trend of development. Still, there is one general case where the entire picture can be substantially affected; illustrations of that exist. The voting of extraordinary resources for military strengthening, as is happening in the Budgets of India and Pakistan, cannot certainly continue without markedly arresting development of the economy; it may even create new economic problems internally and externally in addition to aggravating existing ones. Continuation of similar strains in Burma, Malaya and so on will also have the same result.

To come to actual development work, it is very difficult to find all the financial and capital resources within the economy without restricting consumption levels to slave or famine conditions; besides social conscience, that is not a risk countries will dare to take these days. (Again, it may be interposed, it is possible to go to a slightly greater length in an 'authoritarian' set up than in a 'democratic'). Considerable imports of capital are required. It could be said with truth, that the free availability of capital in the early stages would largely counteract the limiting tendencies of all other factors we have mentioned in the preceding paragraphs. There is Point Four with its promise of technical assistance and of investment



Capital, but the latter is to be only through private investment. What result will really be produced, with the need to create a 'climate' for such imports on the one hand and the urgency to appease 'labour' on the other, is more a matter for conjecture.

Nor is there likelihood of the best trade patterns being created. The compartmentalisation of East and West Europe must now be taken as a datum for economic reckoning. The trade pattern in West Europe seems more likely to continue as it is, with only a tendency to increase internal agricultural production (chiefly food) and thus reduce dollar burdens on that account. The U.S. will be the major exporter of capital to the agricultural countries. The emergence or formation of a South-East Asian Trade Area will be remote—the more so in view of the unsettled political situation in the East generally, and the conflicting ideologies now presented by the advent of communism in China.

The movement forward in a context such as this must certainly be halting, slow, and unpredictable, where every little ill-wind will have a magnified effect. It means that economic theory cannot predict the exact situation in a dynamic movement, with a sureness that astronomy, for example, is familiar with. What we have faced squarely in the preceding paragraphs is what in normal treatments of the subject would be dismissed by the side door with a 'ceteris paribus'. We are not criticising theory. There is no doubt that these limiting factors do not at all affect the validity of the economic policy outlined; a theory can be the only valid one in a given context, though all the results expected of it may not materialise. If then we put ourselves the question whether at the end of a generation the set-up would be as envisaged, we are not sure that it will be so at the end of a generation; it may be less, it may be more. In some countries it will probably be more, while in others like Ceylon it may take about that time. In India, policy in several ways already coincides with that worked out in the Study (though the tempo was too low to produce all the results) and there is a certain ground-work of industrial and capital organisation. With luck two decades may effect most of the necessary change. Much depends on the initial rate of capital importation; free flow of these, together with a planned economic policy could achieve the result in double quick time. Over and



above the logic of economic argument, however, has arisen a new fact which can hardly be overlooked and which may by itself determine the economic picture of the next few decades. It is the re-emergence of 'Asia' on the world stage. If any major upheaval of war were excluded, it is only sound to say that marked and remarkable development in most of the South-East Asian countries and at least a strong buttressing of the structures in the others, are bound to follow. If so, it would probably prevail against most of the hindrances and limitations above mentioned and our theoretical anticipations should be fulfilled even more closely. On the whole, both in 'China' and 'India', the next few decades will probably see marked increase in diversification, industrialisation, employment and standard of living. The movement towards full employment and rising standards will have to be, like it or not, through practically coincident economic, though not political, devices, although operating in slightly varying systems of organisation of units. For our part, we are conscious of the restricted sphere in which our theory of full employment has been worked and we do not pretend any more extended validity for it.

To come back to our own sphere, within whose institutional frame-work the foregoing thesis has been worked out, we may state, in conclusion, that the purpose of correct economic policy is not so much to guarantee cent. per cent results in actual working out, but to ensure movement on the correct lines despite influences and trends to the contrary. The ultimate picture in any situation will, in all probability, be different, in lesser or greater degree. 'No policy', is by no means a substitute; nor, of course, is wrong policy. Correct policy, to repeat, may not create the entire result, but it creates the basic condition for that result. To that extent, the overall economic picture in the future is bound to have much in common with what is considered desirable, though also much that is not—for which, however, economic policy will not be asked to take the blame. In short, economic theory by itself does not achieve a result, but bad theory will, even in a good climate, certainly prevent the expected result. It is in that context that the work of this Study has been attempted and in that that the strength of Theory must also be found to lie.

THE END



## CHAPTER FOURTEEN

### Re-instatement of General Theory

LET it be said immediately that by General Theory we do not necessarily mean the original Keynesian framework outlining the set of forces responsible for a given level of employment in an economy and the devices consequently recommended for stability, especially as expounded in their orthodox form. We, however, would not only admit but emphasize henceforth the applicability of General Theory to agricultural countries; and its necessity for the final emergence and stabilising of full employment. Whatever the additions necessary to the accepted armoury of 'full employment devices' under the Theory, that these devices will come into their own henceforth needs to be strongly recognised for more than one reason. It is useful then to talk of a General Theory—the broad lines of which are certainly accepted almost universally—into which the observations below could be worked.

(i)

At the beginning of this thesis, the point was made that besides severe unemployment there has always been chronic and depressing under-employment. In the course of our study later it was further concluded that in the process of tackling the problem, the objective would be 'standard of living for all' rather than 'employment for all' and that the Development programme would be framed and operated in that context. Theoretically, the programme in organising all resources under a plan, effecting optimal combinations and eliminating surpluses at every stage, should produce two beneficial results. It should exorcise the previous type of under-and unemployment, which we will now refer to as 'endemic unemployment' and it should also produce the maximum standard of living under the circumstances existing. In actual operation, however, two points need to be noted which, jointly, will leave a residue of unemployment in the economy. The rationalisation of the economy in terms of the standard of living will be labour-intensive in comparison to advanced countries. But it will not be 'intensified' to the point of employing more labour than what the given capital equipment requires. In the present state of capital starvation in



- Clark, Collin—Conditions of Economic Progress.
- Clark, Collin—Economics of 1960.
- The Colombo Plan of Economic Development.
- Report of the Consultative Committee (Colombo Plan) on Fourth Meeting (First Annual Report) 1952.
- Census of Ceylon (Published 1951).
- Ceylon Central Bank Report 1950.
- Ceylon Central Bank Report 1951.
- Dalton, H.—Public Finance.
- Dennison—Location of Industry and the Depressed Areas.
- Dobb, M.—Soviet Economic Development.
- Dobb, M.—Political Economy and Capitalism.
- Dobb, M.—Wages.
- Dobb, M.—Studies in the Development of Capitalism.
- Ecafe—Economic Survey for Asia and the Far East, 1949.
- Ecafe—Economic Survey for Asia and the Far East, 1950.
- Ceylon Economic Surveys (Selected Villages).
- Einzig, P.—The Exchange Clearing System.
- Ed. Ellis, H.S.—Survey of Contemporary Economics.
- Feavearyear—The Pound Sterling.
- Finer, H.—T.V.A.—Lessons for International Application.
- Gadgil, D.R.—Industrial Evolution of India.
- Ed. Gayer—Lessons of Monetary Experience.
- Ghate, G.B.—Asia's Trade.
- Gray, A.—Development of Economic Doctrine.
- Gregory, T.E.—The Gold Standard and its Future.
- Das Gupta, B.B.—Economic Survey of Ceylon.
- Haberler, G.—Prosperity and Depression.
- Haberler, G.—International Trade.
- Hansen, A.—Full Recovery or Stagnation.
- Harrod, R.F.—International Economics.
- Harrod, R.F.—Towards a Dynamic Economics.
- Hawtrey, R.G.—Art of Central Banking.
- Hawtrey, R.G.—The Gold Standard.
- Von Hayek—Road to Serfdom.
- Von Hayek—Prices and Production.
- Von Hayek—Pure Theory of Capital.
- Hicks, J.R.—The Social Framework.
- Hicks, J.R.—Value and Capital.
- Hinden, Rita—Plan for Africa.



- Hubbard, G.E.—Eastern Industrialisation & its Effects on the West.
- I.L.O. (H. Butler) Problems of Industry in the East (India, French India, Ceylon, Malaya, & N.E.I.) 1938.
- I.L.O. (Asian Conference '47)—The Economic Background of Social Policy (including problems of Industrialisation).
- I.L.O.—Public Investment and Full Employment.
- I.L.O.—Cost of Living Statistics—Methods & Techniques for the Post-War Period.
- Indian Congress National Planning Committee Reports (Nehru Comm:)
- Indian Council of World Affairs Pamphlets:
- Balasubramanian—A Policy for Agriculture.
- Bhatt—Equal Access to Raw Materials.
- Report of the Indian Government Trade Commissioner for Ceylon, '48.
- Jathar & Beri—Indian Economics.
- Jennings, Ivor—Economy of Ceylon.
- Keynes, J.M.—The Economic Consequences of the Peace.
- Keynes, J.M.—Indian Currency and Finance.
- Keynes, J.M.—Treatise on Money.
- Keynes, J.M.—The General Theory of Employment, Interest & Money.
- Knight, F.H.—Risk, Uncertainty and Profit.
- Knowles—Industrial & Commercial Revolutions in the 19th Century.
- Krishna—Digest of Plans.
- League of Nations—Commercial Policy in the Inter-War Period.
- League of Nations—Economic Stability in the Post-War World.
- League of Nations—The future Population in Europe and the Soviet Union (F. W. Notestein and others).
- League of Nations—Industrialisation and Foreign Trade.
- League of Nations—Quantitative Trade Controls—their Causes and Nature.
- League of Nations—The Transition from War to Peace Economy.
- Lerner, A. P.—Economics of Control.
- Lewis, C.—America's Stake in International Investment.
- Lewis, W. A.—Principles of Economic Planning.
- Lewis, W. A.—Economic Problems of Today.
- Lewis, W. A.—Economic Survey, 1919-1939.



- Lewis, W. A.—Some Aspects of the Flow of Capital into the British Colonies.
- Lokanathan—Eastern Economist Pamphlet No. 1.
- Lokanathan—India's Post-War Reconstruction & Its International aspects.
- Lokanathan—Industrial Organisation in India.
- Rosa Luxemburg—Accumulation of Capital.
- Macgregor, P. H.—Public Aspects of Finance.
- Maini and Others—India Analysed.
- Mandelbaum—Industrialisation of Backward Areas.
- Marshall, Alfred—Principles.
- Marshall, Alfred—Industry and Trade.
- Meade, J. E.—Balance of Payments.
- Meade, J. E.—Economic Analysis & Policy.
- Mills, L. A.—Ceylon Under British Rule.
- Ministers' (Ceylon) Post-War Development Proposals.
- Nag, D. S.—Study of Economic Plans for India.
- Narayanaswamy & Narasimhan—Economics of Indian Agriculture.
- Notestein—Problems of Policy in Relation to Areas of Heavy Population Pressure. (In "Demographic Studies of Selected Areas of Rapid Growth," 1944).
- Norwegian National Budget, 1950.
- Ohlin, B.—Employment and Stabilisation.
- Oxford Economists—The Economics of Full Employment.
- Oxford Pamphlets on Indian Affairs:—
- Chand—The Problem of Population.
- Lokanathan—Industrialisation of India.
- Lorenzo—Atlas of India.
- Mathai—Tariffs and Industry.
- Mukkerjee—The Food Supply.
- Natarajan—Social Problems.
- Shah & Others—The Economic Background.
- Vijayaraghavacharya—The Land & Its Problems.
- Pigou—Keynes' General Theory—a Retrospect.
- Sir Allan Pim—Colonial Agricultural Production.
- Prest—War Economics of Primary Producing Countries.
- Raeburn, J. R.—General Principles of Marketing (from "The Farmer in Business").
- Rao, V. K. R. V.—Essay on India's National Income, 1925-29.



- Rao, V. K. R. V.—National Income of British India, 1931-32.
- Robertson—Control of Industry.
- Robinson, E. A. G.—Structure of Competitive Industry.
- Robinson, J.—Economics of Imperfect Competition.
- Robinson, J.—Essays in the Theory of Employment.
- Ed. Robson—Social Security.
- Ropke, W.—International Economic Disintegration.
- Samuelson, P. A.—Economics.
- Sayers—Modern Banking.
- Schacht, Hjalmar—Gold for Europe.
- Schultz—Agriculture in an Unstable Economy.
- Schultz—Food for the World.
- Schumpeter, J. A.—Capitalism, Socialism and Democracy.
- The Scott Committee Report.
- Sharma, T. R.—Location of Industries in India.
- Sessional Paper XXX, 1951—Report on the visit to the Philippines (Delegation of the Ceylon Coconut Board).
- Sessional Paper 11, 1951—Economic Survey of Rural Ceylon, Preliminary Report, 1950.
- Sessional Paper 11, 1950—Agricultural Wages & Earnings of Primary Producers in Ceylon.
- Sessional Paper XIV, 1949—Report on the Establishment of a Central Bank for Ceylon (J. Exter).
- Sessional Paper VII, 1947—Report on the Social Services (Jennings Committee).
- Sessional Paper XV, 1946—Report on Industrial Development and Policy in Ceylon.
- Sessional Paper VII, 1942—Incidence of Taxation (Gupta).
- Sessional Paper V of 1936—(Ceylon)—Report on the Relief of Distress due to Sickness and Shortage of Food.
- Sessional Paper (C. M. D. 6423), 1943 Labour Conditions in Ceylon, Mauritius and Malaya (Orde Browne).
- Shenoy, B. R.—Sterling Assets of the Reserve Bank of India.
- Shenoy, B. R.—Ceylon Currency and Banking.
- Colvin R. de Silva—Economic History of Ceylon.
- Smith, Vera—Rationale of Central Banking.
- Social and Economic Development of Ceylon, 1926-50 (A Survey)  
Presented to Parliament by the Hon. Min. for Finance.
- Sovani—International position of India's Raw Materials.
- Suriyakumaran, C.—Ceylon, Beveridge and Bretton Woods.



- Swiss Federal Report—(Department of Economics, Agricultural Division)—Les Améliorations foncières de la Suisse 1913-24.
- Swiss Cantonal Report—L'entreprise d'améliorations foncières de la région de Coppet-Nyon, 1934-38.
- Swiss Cantonal Report—of the Société Vaudoise d'Etude et L'Encouragement des Améliorations Foncières, 1945 & 1948.
- Tarlok Singh—Poverty & Social Change; a Study in the economic re-organisation of Indian rural society.
- Tawney, R. H.—Land and Labour in China.
- Taylor, H. C.—Outline of Agricultural Economics.
- Thomas, E.—Introduction to Agricultural Economics.
- Tiwari, R. D.—Indian Agriculture.
- Tse Chung Chang—Cyclical Movements in the Balance of Payments.
- U. N. O. (1947)—Economic Development in Selected Areas.
- U. N. O.—Methods of Financing Economic Development in Under-developed Countries.
- U. N. O.—Maintenance of Full Employment.
- U. N. O.—Relative Prices of Exports and Imports of Under-developed Countries.
- The Utthwatt Committee Report.
- Viner, J.—Studies in the Theory of International Trade.
- Visvesvaraya, M.—Unemployment in India: Its Causes & Cures.
- Visvesvaraya, M.—Planned Economy for India.
- Weber, A.—Theory of the Location of Industries.
- Whale, B.—Joint Stock Banking in Germany.
- Whale, B.—International Trade.
- White Paper (British) on Employment Policy 1944.
- Wootton, B.—Plan or No Plan.
- Wootton, B.—Freedom and Planning.
- Yates, P. L.—Food Production in West Europe.

The chief Journals used were the following:

- Agenda.
- American Economic Review.
- Banker.
- Ceylon Daily News } Daily Papers
- Ceylon Times } Daily Papers
- Eastern Economist, including the Annuals and allied issues.
- Economica.



Economic Journal.  
 Economist.  
 Hindu (Madras)—Daily Paper.  
 Journal of Farm Economics.  
 Journal of the Institute of Bankers.  
 London and Cambridge Economic Service.  
 Modern Review (India).  
 Swatantra (Madras).

The following reference is made to certain relevant articles not cited directly in the Thesis:

Anstey, V.—Economic Reconstruction of India—Agenda, Nov. '43.  
 Cowden, T. K.—Current trends in Agricultural Policy—Journal of Farm Economics, 1949.  
 Harrod, R. F.—An Essay in Dynamic Theory—Econ. Journal, March '39.  
 Hirsch, W. Z.—The Status & Possibilities of Rural Producing Co-operatives—Journal of Farm Economics, 1949.  
 Robinson, J.—The International Currency Proposals—Economic Journal, June-September, 1943.  
 Rowe, J. F. W.—Studies in the Artificial Control of Raw Materials Supplies—Royal Economic Society (London and Cambridge Economic Service) Memo, 1931.  
 Schumacher—Pool Clearing—Economica, May 1943.  
 Whale, B.—International Trade in the absence of an International Standard—Economica, 1936.  
 Whale, B.—Pre-War Gold Standard—Economica, 1937.  
 Whale, B.—International Short-Term Capital Movements—Economica, 1939.  
 Whale, B.—English and Continental Banking, Journal of the Institute of Bankers, 1931.

The following is a list of the authors whose articles in Journals are cited in the Thesis. References to articles in the Economist, Eastern Economist and so on, are naturally not included here:

J. H. Adler—American Economic Review.  
 Agarvala—Free Press Journal (Bombay).  
 H. G. Aubrey—American Economic Review.



- Bauer—Economic Journal.  
Mary J. Bowman—American Economic Review.  
Lord Brand—Economic Journal.  
Y. Brozen—American Economic Review.  
D. H. Buchanan—Economic Journal.  
Chandler—American Economic Review.  
Dunlop—American Economic Review.  
H. Frankel—Economic Journal.  
Haberler—American Economic Review.  
Harrod—American Economic Review.  
Henderson—American Economic Review.  
Hicks—Report of a lecture in Eastern Economist.  
Iyengar—Economic Journal.  
Jaenber—Journal of Farm Economics.  
D. H. Johnson—American Economic Review.  
H. Jones—American Economic Review.  
W. T. C. King—Journal of the Institute of Bankers.  
Klein—American Economic Review.  
Kuznets—American Economic Review.  
W. A. Lewis—Agenda.  
Ragnar Nurkse—American Economic Review.  
Patinkin—American Economic Review.  
Rosenstein-Rodan—Economic Journal.  
Rowe—Economic Journal.  
Schultz—Journal of Farm Economics.  
Silcock—Economic Journal.  
H. W. Singer—American Economic Review.  
Stamp—Economic Journal.  
J. H. Williams—American Economic Review.  
Yuan-Li Wu—Economic Journal.







---

Printed at The Associated Newspapers of Ceylon, Ltd., Lake House, Colombo  
for C. Suriyakumaran of No. 30/2, Kalyani Road, Colombo 6.







