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Introduction

A major development debate from the 1940s to the 1960s concerned balanced growth versus unbalanced growth. Some of the debate was semantic, as the meaning of balance can vary from the abrupt requirement that all sectors grow simultaneously and at the same rate to the more simple plea that same attention be given to all major sectors—industry, agriculture and services.

In contrast, A. O. Hirschman develops the idea of unbalanced investment to complement existing imbalances. A broad choice of development strategy is between Ragnar Nurkse's theory of balanced growth (BG) and A. O. Hirschman's theory of unbalanced growth (UG). The doctrine of BG is based on the economic rationale for a 'big push'.

By contrast, UG is based on the hypothesis that a 'big push' or a 'critical minimum effort' is not feasible. So the best way to stimulate development in LDCs is to deliberately create an imbalance. The issue is yet to be resolved. So, there are two opposite issues on development strategy.

The origin of the idea of balanced growth can be traced back to the 200-year old Say's Law of Markets (1803)- Every increase in production, if distributed in the correct proportion among the factors of production on the basis of their respective contributions to society's output, creates its own demand. Say made an insightful analysis that all productive activity creates demand along with supply.

J. S. Mill added (1848) that while production creates specific supplies, and investment creates specific productive capacities, the income they generate creates general demand, which, then, is distributed over many goods.

This hypothesis has an important implication. If the structure of additional productive capacities is to match the structure of additional demand, investment would have to proceed simultaneously in the various sectors of the economy and industries in the same proportions in which the consumers decide to allow the expenditure of their additional income among the outputs of those sectors and industries.

This implies a faster growth of sectors and industries which produce goods having high income elasticities of demand and a simultaneous but slower growth of industries producing goods having low income elasticities of demand. This is the essence of balanced growth.

Different Interpretations of the Term ‘Balanced Growth’:

The synchronized application of capital to a wide range of different industries is called balanced growth by its advocates. The term BG is used in different senses. Paul Rosenstein Rodan, one of the original proponents of the doctrine, had in mind the scale of investment necessary to overcome indivisibilities on both the supply and the demand sides of the development process.

Indivisibilities on the supply side refers to the ‘lumpiness’ of capital (especially social overhead capital) and the fact that only investment in a large number of activities simultaneously can exploit the various external economies of scale.

Indivisibilities on the demand side refer to the limitations imposed by the size of the market on the profitability, and thus economic feasibility, of various productive activities in the private sector. Thus, the doctrine of BG was originally interpreted as the large-scale expansion of economic activities to overcome divergences between private and social return.

Nurkse (1953) had extended the doctrine to refer to the path of economic development and the pattern of investment necessary to keep the different sectors of the economy in balance, so that lack of development in one sector does not act as an obstacle to development of others.

Nurkse considers this strategy the only way of escaping from the vicious circle of poverty. Of course, it is not necessary for output in all sectors to grow at the same rate, but, rather in accordance with the income elasticity of demand for products, so that supply equals demand at the micro-level.

This implies equilibrium in the market for each commodity as also absence of shortages and bottlenecks of any type. He does not consider the expansion of exports promising, because the price elasticity of demand for the LDCs’ predominantly primary exports is less than one, thus reducing export earning with increased volume, other things being equal.

Horizontal vs. Vertical Balance:

BG, therefore, has both horizontal and vertical aspects. On the one hand it recognises indivisibilities in supply and complementarities of demand. On the other hand it highlights the importance of achieving balance between such sectors as agriculture and industry, between the consumer goods industries and the capital goods industries, and between social overhead capital (SOC) and directly productive activities (DPA).

Two Versions of Balanced Growth:

Thus, there are two versions of the doctrine of BG. One refers to the path of development and the pattern of investment necessary to ensure smooth functioning of the economy. The other refers to the scale of investment necessary to overcome indivisibilities in the production process on both sides of the market. Nurkse’s exposition of BG embraces both versions of the doctrine, while Rosenstein-Rodan concentrates on the necessity for a ‘big-push’ to overcome the existence of indivisibilities.

On the demand side, the division of labour is limited by the size of the market and if the market is limited, certain activities may not be economically viable. So, several activities are to be set up simultaneously so that each can provide a market for the others’ products. In addition, activities that are not profitable, when considered in isolation, will become so when considered in the context of a large-scale development programme.

For this it is necessary that industrial enterprises are of a certain minimum size so that they can operate profitably. On the supply side, the argument for a 'big push' is inseparably linked up with the existence of external economies of scale.

In the context of development economics, the external economies refer mainly to the impact of a large investment programme on the cost and profit functions of the participating firms. In the presence of external economies, in either sense, the social return of an activity will exceed the private return.

The only way to eliminate this divergence is to make each activity part of an overall programme of investment expansion. Industries or enterprises which are unprofitable, when considered in isolation, become economically viable when considered as part of a comprehensive plan for industrial expansion embracing several activities.

No doubt, certain investments have to be of a minimum size to be economically feasible. It may be uneconomical to build roads, highways, buildings, railways and power plants if the current level of demand for transport services and power is low due to the backward nature of the economy.

This type of SOC should be built on a large scale in order to achieve long-run economy in the use of resources only when different industries are set up simultaneously and the demand for SOC increases.

Intersectoral Balance:

The second version of the theory of BG stresses the necessity of balance among different sectors of the economy. The objective is to prevent development of bottlenecks in some sectors, which may act as an obstacle to development and excess capacity in others which may be wasteful. For example, a shortage of raw jute or raw cotton will hinder the development of the jute or the cotton textile industries.

Similarly, a shortage of steel may hinder the development of the automobile industry or even the engineering industry. This is why Nurkse (1953) and Arthur Lewis (1954) placed particular emphasis on achieving balance between the agricultural and the industrial sectors of LDCs.

Two main reasons explain how the two sectors mutually exist and stimulate each other:

1. A balance between the agricultural and consumer goods sectors is necessary to give incentives to the farmers to improve productivity so as to expand their marketable surplus. If the consumer-goods sectors do not develop, the demand for agricultural goods will not increase much.
2. For increasing agricultural productivity there is need for capital goods such as tractors pump sets, etc. This requires a balance between agriculture and capital goods producing industries. Moreover, without good roads, farmers cannot sell their products in open markets at fair prices. So, there is need to provide adequate SOC in the form of roads, highways, buildings, etc.

The doctrine of BG stresses on the balance between agriculture and industry for three other reasons:

3. Agricultural output can provide a basis for the development of agro-based local industries.

4. The industrial sector depends on the agricultural sector for food.
5. In the absence of increasing exports, the agricultural sector has to rely on the industrial sector for absorbing a major portion of its products.

Criticisms of the Doctrine of Balanced Growth:

1. Shortages of Resources:

The main criticism of the doctrine of BG is that it fails to tackle, perhaps, the most serious obstacle to development of LDC, viz, a shortage of resources of all kinds. The truth is that if LDCs do possess the resources for a 'big push' they ought not to be described as LDCs in the first place.

No one can deny the importance of a large-scale investment programme and the expansion of complementary activities. But in the absence of adequate resources, especially, capital, entrepreneurs and decision-makers, the adoption of the policy of BG may not provide a sufficient stimulus to the spontaneous mobilisation of resources or the inducement to invest.

2. BG on a Global Scale:

The doctrine of BG calls for inward-looking development policies- investment in productive capacities to match the expansion of domestic demand. It then conflicts with the theory of comparative advantage, which says that rather than producing everything at home, each country does better through specialisation in the production of goods in which it is relatively efficient and by importing other goods in which it is relatively inefficient.

3. Economies of Scale:

The doctrine of BG also conflicts with the arguments for exploiting economies of scale. Whenever a country's domestic market for a particular good is too small to absorb the minimum output that is economical to produce it is cheaper for it either to import that good from high-volume low-cost producers abroad, or to produce it at home on a large enough scale to render its cost competitive in world markets and export the surplus. This means that growth would have to be balanced, not on a national but on a global scale. This view has been expressed by T. Scitovsky.

The most influential advocate of BG was of course, Nurkse, who put the following argument:

The case of international specialisation is as strong as ever. But, if development through increased exports to the advanced countries is retarded or blocked, there arises a possible need for promoting increases in output that are diversified in accordance with domestic income elasticities of demand so as to provide markets for each other locally.

No doubt there was widespread agreement on the desirability of matching the structure of output to the structure of domestic demand. But there was widespread disagreement (in the late 1950s) as to the best way to achieve that goal. Nurkse and his followers believed that, in poor countries, the market, left to itself, perpetuates poverty, because to escape from it would require investment in increasing productivity.

This is impeded not only by the low saving of the poor but even more by the lack of profit incentive to build high-productivity plants when the already existing local market for their output is too small.

As a means of escaping from that vicious circle, Nurkse advocated the BG doctrine. BG can be achieved in two ways. First, careful planning of investment can overcome the lack of private incentive. Alternatively, indicative planning can provide enough additional incentive, especially when aided by tariff protection, tax concessions or cheap credit.