
UNIT 1 CHANGES IN THE AGRARIAN STRUCTURE: CLASSICAL SERFDOM TO SECOND ENCLOSURE

Structure

- 1.0 Objectives
- 1.1 Introduction
- 1.2 Classical Serfdom—Lord and Peasants
- 1.3 Low Productivity under the Manorial System
- 1.4 The Feudal Crisis
 - 1.4.1 Inability to Increase Agricultural Output
 - 1.4.2 Increased Feudal Exactions
 - 1.4.3 Flight of Serfs
 - 1.4.4 Emergence of Yeomanry
- 1.5 The Sixteenth Century Price Revolution and its Economic Impact
- 1.6 The Enclosure Movement of the Sixteenth Century
 - 1.6.1 Enclosures—Consolidation of Agricultural Land and Creation of Pastures
 - 1.6.2 Implications for Poor Peasantry
 - 1.6.3 Poor Laws, Laws against Vagabondage and Laws to Keep Wages Down
 - 1.6.4 Enrichment of Well-to-do Peasantry
- 1.7 The Seventeenth Century Civil War and Changes in Land Relations
- 1.8 Free Wage Labour in the Seventeenth Century
- 1.9 Enclosure of Commons—Eighteenth and Early Nineteenth Century
- 1.10 Investment, Technical Change and Productivity Increases—The Agricultural Revolution
- 1.11 Let Us Sum Up
- 1.12 Key Words
- 1.13 Some Useful Books
- 1.14 Answers/Hints to Check Your Progress Exercises

1.0 OBJECTIVES

After going through this unit, you will have an idea of:

- the classical serfdom of medieval England
- technological and socio-economic factors causing low productivity in the feudal economy
- the reasons behind the feudal crisis in agriculture, and
- the rise of capitalist tendencies in agriculture resulting in changes taking the dimension of an agricultural revolution.

1.1 INTRODUCTION

The period between the sixteenth and eighteenth century in Britain witnessed substantial changes in the sphere of agriculture which had far reaching implications for subsequent developments. The impact of these changes both facilitated and caused a fundamental transformation, not only of agricultural production and organisation, but were essential preconditions for the Industrial Revolution in particular and industrialisation in general. Industrialisation necessitates a rise in agricultural productivity so as to ensure the availability of foodgrains for the industrial workers at prices which are low enough not to exert an upward pressure on wages. Moreover, the productivity of agriculture needs to rise by an extent which would at least compensate for the movement of large masses of population out of agricultural production to the centres of industrial activity as wage labour. Finally, an increase in productivity of foodgrains which lead to stable and low prices would, by lowering costs of subsistence, leave some purchasing power in the hands of the worker and thereby result in the creation of a home market for industrial output.

Changes in the agrarian structure in this period also led to the creation of 'free' wage labour characterised by a dual freedom. First was freedom from the ownership of or access to means of production and subsistence, so that labourers owned nothing but their ability to perform labour i.e. 'labour power'. The second aspect of freedom related to the freedom to sell labour power to anyone, by entering into a wage contract without any extra economic compulsion being exerted on them.

Simultaneous with the emergence of the vast majority of propertyless wage labour was the concentration of much of the productive resources of society in the hands of a small minority as private property. This minority organised production employing hired labour against wage payment was a precondition for increasing agricultural productivity.

This unit outlines the main features of a long and complex historical process which eventually culminated in the industrialisation of Britain. The developments in agriculture and changes in the agrarian structure over the centuries were in many senses critical for the possibility and pattern of subsequent developments, as we shall see below.

1.2 CLASSICAL SERFDOM—LORD AND PEASANTS

By the 12th century the system of the great estate, or **manor**, was at its height throughout Europe. Independent peasant cultivators never completely disappeared and were present in large numbers especially in the periphery of the expanding cultivation frontier. But the majority of peasant cultivators by this date were dependent and **enserved**, that is, tied to the great estates of feudal lords and subject to the payment of **rent** for permission to cultivate their own farms for their own subsistence.

While the great medieval estates varied in size, on average they seem to have contained three hundred farms (**Mansi**) or about 10,000 acres. These farms of the peasant serfs were never together in adjacent villages, but often scattered over several villages and over great distances. The manor of a lord might thus contain farms of serfs in several villages, and different groups of the inhabitants of a given village might owe allegiance to different lords. Thus the 'unitary manor', or the manor whose lands were all in one or more adjacent villages, was the exception rather than the rule. This scattering arose from accidents of conquest and inheritance.

The cultivated land in a manor was termed the **arable**, as distinct from pasture and forest which was used in common by everyone. The arable in turn was divided into the **demesne**, or the domain land directly under the lord, and the serf farms. There were varying degrees of servitude of the peasants to the lord depending on the historical origin of the peasant's status. There was a group of persons who served the lord and his household, who were virtually slaves (**mancipia**). The majority of the

cultivating peasants were semi-free in that their persons could not be bought and sold; but on the other hand they could not move from the manor without permission. They owned oxen and implements, and were permitted to cultivate their own plots of land which they occupied, provided that they paid rent to the lord. The form of rent could be (a) labour-services, viz. the performing of unpaid labour on the lord's demesne land or in handicraft production; (b) kind rent, such as supplying specified amounts of various kinds of produce of the serf plot to the lord; and (c) cash rent, namely a sum of money. The size of the serfs' farm varied with the productivity of land and was such as to give just a customary subsistence. Another category of serfs were poorer than the average. They were termed cottars and as their plots were very small, they worked as hired hands for other serfs and on the demesne.

The commonest form of rent payment during classical feudalism was (a), labour-services. This was frequently combined with a multitude of kind payments as well as some cash payment. Towards the later part of the medieval age, kind and cash payments supplanted labour-services more and more, with the Lord cultivating the demesne with hired labour rather than with labour services.

The lord resided in a fortified manor house with this extended household including large numbers of personal servants and retainers. Some serfs were put in a privileged supervisory position over others and charged with managing the lord's demesne land cultivation, or his herds of swine or geese. The manor house was surrounded by barns, gardens and vineyards, and by the gynecae or workshops in which articles of daily use such as cloth and footwear were fabricated by the labour-services of serfs, for the use of the lord's household. The lord also ran a mill powered by water for grinding corn, and it was obligatory for the serfs to grind their own corn for a payment at this mill. The lord had a monopoly of the brewery for brewing ale for which the serfs had to make a payment.

It will be clear from this description that to a substantial extent, the great estate was a self-sufficient economic unit producing most of what it required directly and selling only the surplus production on the market. The attempt to be self-sufficient in fact led to the great lords acquiring distant land which might be suitable for growing a particular product which could not be grown locally. The monasteries were also big feudal landowners, and many monasteries in France transported their wine from villages under their jurisdiction which might be upto 600km. distant. This is one example of the wastefulness of the manorial system. Equally important was the low productivity and inefficiency of medieval agriculture.

1.3 LOW PRODUCTIVITY UNDER THE MANORIAL SYSTEM

Over most of Europe except the lands bordering the Mediterranean, the agricultural season is very short owing to the long cold winter, so that only one crop could be grown. The period of fallow had to be long to enable the soil to recover its fertility as enough organic manures could not be produced. This was a result of the inability to raise enough fodder crops to feed livestock through the winter months when natural grazing land was frozen or snow-covered. The ratio of seed to yield in crop production was also very high. Thus we may identify the following factors in the low productivity of medieval agriculture in Europe:

Long fallow period: Under the 2 field system of rotation, only one field in a year was sown while the other lay bare with the sequence being reversed the next year. Thus under this system half the arable land lay uncultivated at a time. Under the 3-field system of rotation, of three fields two were sown to crops in a given year while the third lay fallow. Under this system one-third of the arable was uncultivated at a time.

High seed-yield ratio: The proportion of the grain harvested which had to be set aside for seed for the next period was very high in the early medieval period at between one-third to two-fifths of total output. Towards the later period the ratio declined somewhat but the best proportion in the 15th-16th century was still 20 to 25

per cent. This meant that net output available for consumption was much lower than in the tropical agriculture of Asia, for example.

Inadequate livestock feed: Natural grazing provided most of the livestock feed and since this was not available during the winter months, ideally fodder crops which could be stored, were required. Given the low productivity in grain production, the output was barely enough to feed humans, and in the absence of adequate fodder stocks large numbers of livestock had to be slaughtered for meat at the onset of winter. This reduced the potential output of organic manures which when applied to the fields could have helped to reduce the period of fallow, intensify cultivation and raise grain output. The cycle of low productivity was perpetuated. Meat had to be heavily salted and spiced to preserve it through winter, and spices had to be imported from Asia.

Strip farming in open fields: A field producing a given crop was divided into a number of long strips, each belonging to a different serf household. Often the lord's demesne land also lay intermingled in strips amongst the peasant strips. This practice of strip cultivation probably arose from the distribution of a given quality of land among all the households. The fields were not fenced or enclosed. The decisions regarding crop rotation were taken by the peasants as a body, and at the end of the harvest all the livestock were let loose to graze on the stubbles.

One result of strip farming was that a lot of time and labour was wasted in going with plough and oxen to several fields by each household. Arable area was wasted in a larger number of 'plough turns' (the space required by oxen to turn the plough at the end of a strip). No one could experiment with a new cropping pattern or try out a new crop owing to the open fields where livestock roamed freely at the end of the traditional harvest. Strip farming thus contributed to the wastefulness of medieval agriculture.

A short calculation will show that under the two field system, out of every 100 acres of arable land only 50 would be under cultivation in a given year. Suppose that this produced 50 units of grain output, with a seed-yield percentage of 40, as much as 20 units would go as seed and only 30 units of net output would be available for consumption by humans and livestock. In a modern system of agriculture where fallow is, say 10 per cent of cultivable area, and the seed-yield ratio is also 10 per cent, the corresponding net output from 100 acres of land would be 81 units! Thus medieval agriculture at its most inefficient stage produced just over one-third of the net output of modern agriculture (actually much less, for crop varieties and techniques are taken as constant in the calculation). Given this low productivity we realise that even with the rent from 300 serf farmers to support the consumption of his household, the average feudal lord of the estate in Europe probably felt impoverished when he heard of the ostentatious consumption of Asian potentates.

Socio Economic Aspect of Agrarian Structure

As discussed in Section 1.2, underlying the distribution of arable land between the Lord and peasants was the performance of free labour services or payment of rent in cash or kind to the Lord. This was established by custom and enforced by actual/potential force.

The extraction of rent from the peasantry by the Lords often wiped out surplus income. This meant that the peasants were not left with sufficient funds for undertaking improvements in productivity through investment.

Furthermore, rent exactions also made inroads into the funds meant for preservation of fertility of peasant holdings. One of the first casualties, in this context, was the application of natural manure. Given the acute paucity of investible funds, the peasants were unable to purchase new livestock or take adequate care of those they did own. Add to this the insistence of the Lord that all the manorial sheep be folded on demesne plots.

The Lords had the required surpluses required for investment in raising productivity. Further, better techniques not only existed, but their superiority was established. But the social structure did not make it essential for the Lords to raise productivity in order to raise incomes—they could, and did increase incomes by increasing rental

1.4.1 Inability to Increase Agricultural Output

The increased need for revenue could not be met by agriculture. This was largely for two reasons. Firstly, although much colonisation of new land took place there were limits to the expansion of cultivated area beyond a point. Secondly, as seen earlier, there was little scope to increase productivity (output per unit of area) given the social structure and organisation of production.

In part, increased exactions were sought to be met by bringing new land under cultivation. This was facilitated by an increasing population till 1300. In fact, till the beginning of the twelfth century, only one fifth of the land cultivated at present was under cultivation in England (compared to half in France and one third in Germany at that time). The rest was forest, wasteland and heath. Large areas of this land was cleared and cultivated in this period, on condition of an rent-free period with a subsequent payment of rent by the new cultivators. This new land usually carried a money rental as against labour services or kind rents.

However, by the end of the 13th century, the evidence indicates that the extension of cultivated area lagged behind population increase. Further expansion required heavy investment in drainage, dike-building in the case of the Lowlands, of a magnitude which was not forth-coming within the existing system.

1.4.2 Increased Feudal Exactions

Given the lack of means or incentives to improve productivity, and inability to extend cultivated area beyond certain limits, the lords increased the extraction of rent from the peasantry. This enhanced burden on the peasantry cut into their subsistence, and threatened their very survival. The crises both contributed to and was aggravated by the demographic collapse of the thirteenth century.

In the great plague, termed the Black Death of 1348 which swept over Europe, it is likely that the poor majority of the working population had a much higher proportion of deaths than the well-to-do, given their subjection to a long period of poor nutritional status. This, in turn, had its roots in stagnant productivity and rising feudal burdens of the preceding decades. The strong demographic impact of the Black Death is evident from the fact that twice as many people died from it in fourteenth century Europe than during the first World War in twentieth century Europe. In London, about 200 people died every day, and as high as between one-third and one-half of England's total population died.

1.4.3 Flight of Serfs

Burdened by heightened feudal pressures, the serfs resorted to large scale illegal flight to the towns, which led to an increase in the urban population. It also resulted in the increase in gangs of outlaws and bandits, as well as of vagabonds who roamed the country side.

The Lords reacted in two ways. The first was to enter into agreements with each other to help capture fugitive serfs. This was particularly important after the decline in population. Where the alternative in the form of hired labour existed, however, for example where there was a high proportion of cottagers, the Lords preferred to convert labour rent into cash rent. This was termed the 'commutation' of labour-services. They then cultivated demesne land directly using hired labour. There was also a tendency towards conversion of kind rents into cash rent with the commutation of labour services.

1.4.4 Emergence of the Yeomanry

The term 'yeoman' was popularly used by the 16th century for any well to do farmer, whose condition lay between that of the poor cottager or peasant and the rich gentleman. There is evidence of a growing differentiation amongst the peasantry, with the rise of a strata of well-to-do peasants, at the expense of the vast majority of impoverished peasants with meagre holdings. This can be traced to a number of factors:

- a) Some peasants reap the benefits, over decades of access to superior quality land
- b) Some benefited by virtue of being manorial officials

- c) Village poverty allowed the village usurer and petty employer to flourish.
- d) The commutation to cash rents benefited the peasants able to produce a surplus; because the cash rents were fixed over long periods, while output prices were rising during the 16th century in particular (see Sec. 1.5 below) so that rent formed a progressively smaller part of output. These peasants could invest the surpluses they retained and raise incomes.
- e) Consolidation of holdings through strip swapping aided the ability of better-off farmers to farm more efficiently, using the hired labour of their more impoverished neighbours.

All this contributed to this section's purchase of free land, and while differentiation also existed on village holdings, it was most marked on free holding.

The emergence of the well to do middle peasants, as well as commutation of peasant labour rent to cash rent altered the Lord-Serf relation. The serf became more and more like a tenant. Now, he could benefit from increases in productivity or price, since the rents were fixed. Cash rents remained customarily unchanged over decades. Moreover, a section of the peasantry had the means to bring about productivity enhancing changes through investment. It can therefore be concluded that by the sixteenth century serfdom in the earlier sense had disappeared. It must be remembered, however, that the tenures were still feudal and were held "by the custom of the manor".

Check Your Progress 2

- 1) What was the nature of rent paid in the feudal economy? Over time, how did it undergo a transformation?

.....
.....
.....
.....

- 2) Who is a 'yeoman'? How did this category of peasantry emerge over time?

.....
.....
.....
.....
.....
.....

- 3) What are the different avenues by which the landlords increased feudal exactions? What was the serfs' response to it?

.....
.....
.....
.....
.....
.....
.....
.....
.....
.....

1.5 THE SIXTEENTH CENTURY PRICE REVOLUTION AND ITS ECONOMIC IMPACT

The discovery of the New World, and of the civilisations of the Inca of Peru and the Aztec of Mexico by Spain opened up European access to their rich gold and silver mines. These civilisations were conquered, their rulers killed and many of their subjects enslaved. The existing hoards of precious metals were plundered by the Spanish Conquistadores and the mines were now worked using cheap slave labour, which led to a substantial fall in the cost of production of precious metals compared to the cost of production in European mines. There was a huge inflow of these metals to the European continent in the first instance to Spain and Portugal and then through trade to the rest of Europe.

Table 1.1 : Influx of Silver into Sixteenth Century Europe

Silver Influx Year	Quantity (kgs.)
1500-1520	45,000
1545-1560	270,000
1580-1600	340,000

Source : Leo Huberman (1946). *Man's Wordly Goods*, p.101.

The combination of a large increase in the supply of the precious metals and their cheapening, led to a rapid increase in the general price level of other goods which was so far-reaching in its impact that it has been called a 'price revolution'. By modern standards the inflation rate may seem low but in the context of centuries of price stability it was indeed revolutionary.

However, had all prices increased at the same rate, then even a very high rate of inflation would not have had much impact on the social structure. This was not the case; in England, while the general price level doubled in the course of the 16th century, all prices did not rise in tandem. This resulted in an alteration of the relative prices of different goods and services. The price of necessities rose faster than other prices. This was especially true of agricultural prices, with the terms of trade moving sharply in favour of agriculture. This had two immediate implications.

Firstly, an increase in the price of necessities like food in the face of more sluggish wage increases implies a fall in real wages. This implies an increase in profits for the employers of labour in producing goods whose prices are rising faster than money wages. In fact, J.M. Keynes in his *Treatise on Money* terms the 16th century price inflation, as one of the earliest 'profit inflations'.

Secondly, the profitability of agricultural production increased particularly since the price of agricultural produce rose more rapidly than other prices. Let us enumerate the losers and beneficiaries of the price inflation:

The Losers

The wage earners lost out despite an increase in their money wages, owing to a faster increase in the prices of wage goods like food so that they experienced a decline in real wages.

Landlords lost out both owing to a decline or less rapid increase in land prices, as well as owing to fixity of cash rents in long duration leases.

The state coffers lost out owing to stickiness of money revenue collected and a consequent decline in its value in real terms.

The Beneficiaries

All employers of hired labour in towns benefited owing to a decline in real wages. So did the rich peasants and tenants with fixed money leases for long durations, since rent remained constant in money terms while all other prices rose. They also gained

through favourable terms of trade for agricultural output. Merchants benefited from an increase in trade margins of goods whose prices had increased.

Moneylenders benefited from loans made out to those who were in distress in the changed circumstances, which included a section of the rentiers as well as the poor peasantry. In this way there was a transfer of income from wage earners and rentiers to those earning profit incomes like merchants and rich peasants.

Rack Renting, Tallage and Entry Fines

As discussed earlier, the most obvious solution for the landlords faced with rising revenue needs and falling real incomes was to pressurise peasant subsistence by raising rents, tallage and entry fines. Though these were supposedly guided by what was called the "custom of the manor", it was interpreted to mean "by the will of the lord". Thus manipulation of entry fines (at the time of inheritance or purchase of land) was used as an instrument to raise rents. The Price Revolution had a direct bearing on the Enclosure Movement as we shall see in the next section.

1.6 THE ENCLOSURE MOVEMENT OF THE SIXTEENTH CENTURY

'Enclosure' literally referred to the fencing of hitherto open fields; but it had much wider social consequences than this would suggest because it was accompanied by an appropriation of common lands and marginalisation of ordinary cultivators. The landlords in the 16th century in particular enclosed the open fields in large units as agricultural production became profitable. It resulted in eviction of the peasants from the lands they had cultivated for generations. The Enclosure Movement was an expression of the rising capitalist tendencies in English agriculture as we shall see below:

1.6.1 Enclosures—Consolidation of Agricultural Land and Creation of Pastures

Agricultural production became profitable because of favourable terms of trade for agriculture as well as increased demand for domestic production of corn from the rapidly growing urban centres. Strip swapping as well as purchases through distress of small peasants and/or overt force resulted in consolidation and enclosure of cultivated land. This facilitated investment in improved techniques of production and hence increase in productivity when owned or leased by rich tenants or the few landlords who viewed agriculture as an avenue for investment. The relative importance of rack renting and entry fines is considered more important as a source of increasing feudal revenue in this period. But the more critical development in terms of its future implication was the enclosure of arable land and its conversion to pastures.

There was a phenomenal growth in wool manufacture in Flanders, which substantially raised the profitability of raising sheep to export raw price of wool in England. A direct consequence of this was the large scale eviction of thousands of peasants from the cultivable land on which they had customary control, and the conversion of the land so enclosed into grazing ground for sheep.

The enclosure affected 25 counties and 2% to 4% of total area, or 5% to 10% of cultivable area. However, in the four most affected counties, 10% of the total or a third of the cultivable area was enclosed, directly affecting half the population. The estimate for the area enclosed between 1455 and 1607 is estimated by one authority to be about half a million acres, and numbers thrown out of employment to be 30,000 to 40,000 between 1455 and 1637. No wonder then, that Sir Thomas More referred (in his *Utopia*) to the hitherto meek English sheep which had grown so fierce as to eat up men!

It may be noted that these enclosure were carried through by private violence of the profit-minded gentry and were in complete contravention of the Tudor law. The

entire 150 year period beginning in 1498 is replete with legislation to put a halt to depopulating enclosures of arable land and the consequent evictions. The regular re-enactment of the law is itself proof of its ineffectiveness, and even commons were sometimes enclosed by the landlords with impunity.

The reason for the success of the gentry in contravening the law was twofold—the incentive of a four to seven fold increase in income from sheep rearing, and the poverty of the poor peasantry who could not afford lengthy and expensive legal battles. Often the economic distress of the landlords prompted the sale and/or mortgage of land to city merchants and rich farmers. In this way, we can see that feudal values had increasingly and decisively been replaced by the capitalist profit motive.

1.6.2 Implications for Poor Peasantry

The poor peasants suffered from distress in the following ways :

Burden of Rising Feudal Exactions : The peasants had to increasingly bear the huge burden of feudal exactions imposed by the landlords.

Fall in Real Wages : A decline in real wages implied a reduction in the supplementary incomes of the poor peasantry through wage labour.

Indebtedness : Poor peasants who had declining real incomes, were forced to take loans at usurious rates of interest. These were usually from richer neighbours, who extended credit with an eye on the land of the poor.

Distress/Forced Sale of Land : The poor were also forced, either by their economic circumstances, or through overt violence, to sell their land at very low prices.

Eviction : The most critical factor which led to the dispossession of the poor peasantry was the large scale uprooting of the populace settled on enclosed arable land.

Decline in Access to Commons : The enclosure of some pasture and woodland resulted in a loss of access to some extent from timber, animal hunting etc. This must have been critical for those at the margin of survival.

Vagabondage, Begging : Apart from wage labour, the burdened poor peasantry resorted to mass flight to escape feudal exactions etc. which gave rise to thousands of vagabonds, beggars etc. scouting the countryside (discussed below). Nearly 80,000 people also left England between 1620 and 1642 for the New World.

1.6.3 Poor Laws, Laws against Vagabondage, and Laws to Keep Wages Down

The dispossessed poor were not only thrown onto the labour market, but subject to a series of laws which restricted both their mobility and their earnings. The mass scale flight of the erstwhile poor peasantry and recourse to vagabondage, begging and robbery was detrimental to the interests of the emerging rich peasantry in the countryside as well as the new centres of hired labour based manufacture. A number of laws were enacted to tie down the peasantry to their employers, and force them to work at extremely low wages. A brief sample of this legislation is presented below:

1530 : Old and infirm beggars were to be issued licences, whereas all other vagabonds and paupers were forced to return to their place of birth or place of work of the previous three years. On being arrested for the third time, the offender was to be executed as a hardened criminal.

1572 & 1597 : Unlicensed beggars above the age of 14 years were to be executed if caught the third time.

The laws presented above are indicative rather than exhaustive. After 1563, poor rates and poor relief could be given, though it was not done in all the parishes. Though viewed with immense disfavour by the propertied, this relief was motivated more by the necessity to subsidise wages rather than philanthropy. In times of

scarcity the poor relief ensured a bare minimum subsistence and thus prevented starvation and revolts. Hence, these Laws were a method to tie reserves of labour in the countryside, keep wages low and impose discipline on the poor in its transition from a class of possessing and independent peasants to a class of "free" wage labour. As far as wage labour was concerned, the legislation commenced with the Statute of Labourers, 1349. Wages were fixed on daily as well as piece-rate basis for the towns and the countryside. Agricultural labourers were compelled to be hired by the year, and the town labourers in the open market. Imprisonment resulted for paying wages higher than those fixed by statute, but the receipt of higher wages was more severely dealt with than its payment. In the sixteenth century real wages fell but nevertheless the laws regulating maximum wages was strictly enforced. It was only as late as 1796 that a law regulating minimum wages was passed. This, not surprisingly, was not implemented, an anomaly facilitated by the various laws opposing unionisation of the workers to enhance their bargaining power.

No wonder, then, that by the end of the sixteenth century the victim of the enclosure was generally the smaller cultivator, who now dispossessed was doomed to swell the ranks of the rural, proletariat or semi-proletariat, gaining employment as a hired labourer if he was lucky and being hunted by the cruelties of the Poor Law if he was not. The enclosures were therefore the first step in the creation of free wage labour.

1.6.4 Enrichment of Well-to-do Peasantry

The price inflation and enclosures strengthened the position of the rich peasantry. This was done in a number of ways :

- 1) Acquisition/Purchase of land, both from distressed big landlords and small peasantry.
- 2) Leasing of large quantities of land on long-term fixed cash rent basis.
- 3) Consolidation of holdings and evictions, in a manner similar to the Lords.
- 4) Through hired labour based farming and decline in real wages.
- 5) Investment in enhancing productivity both on leased plots as well as owned plots.
- 6) Gains from usurious interest from loans to poor neighbours.

Check Your Progress 3

- 1) Why was there a rapid inflation in the Sixteenth Century England? Did prices of commodities increase in the same proportion? In which direction did the share of wages move?

.....
.....
.....
.....
.....
.....
.....
.....
.....

- 2) Briefly outline how the agricultural land was enclosed. What was the impact of the Enclosure Movement on the poor peasantry?

.....
.....
.....
.....
.....
.....
.....
.....

- 2) Did the first wave of enclosures lead to an immediate creation of large reserve army of 'free' labour? Explain.

.....

.....

.....

.....

.....

.....

.....

.....

1.9 ENCLOSURE OF COMMONS—EIGHTEENTH AND EARLY NINETEENTH CENTURY

The last Act against depopulating enclosures was enacted in 1597, a famine year. 1608 saw a limited pro-enclosure bill, while 1621 heralded in the first general enclosure bill. Finally, in 1624 the statutes against Enclosures were repealed, though in the late twenties some attempts were made to make money by fining enclosures. After 1640, no serious attempts were made to either prevent or fine enclosures. Throughout the seventeenth century, enclosures continued, though with less drastic results since it accompanied some reversion from pasture to tillage. The anti-enclosure position of the Tudor and Stuart governments contrasts strongly with the pro-enclosure actions of the State after the Civil War.

The extent and pace of enclosures accelerated sharply in the eighteenth and early nineteenth century, with the enactment of several bills for the enclosure of land held in common, which culminated in the clearing of cottages. It is important to stress that now the enclosures were enacted by Acts of Parliament.

The second round of enclosures, brought about by law, were much more powerful in terms of the area affected. The percentage of commercial land and some wasteland enclosed in the eighteenth century was as high as 25% to 50%. Further, in only 16 of the 36 countries the percentage of land enclosed was less than five. Between 1700 and 1850, grain output rose by about 120%, whereas yields improved by about 25% to 50%. In the same period, livestock (including sheep and cattle) rose by 150%. The significance of this increase is brought out clearly when compared to previous periods.

In the fourteenth century, agriculture supported a home population of 2.5 to 3 million people. By 1700, home production supported a population of 5.8 million. The end of 1850 saw domestic agriculture support 80% of the now increased population of 17.8 million people.

As mentioned above, increase in yield accounted only for a third of the increase in output. The expansion of cultivated acreage was done in a number of ways. The methods adopted included drainage of marshes (the drainage of Fens alone increased England's arable land by 10%); deforestation and subsequent cultivation of forests; cultivation of heath and wasteland; cultivation of commons etc.

The most important way in which productivity was enhanced and the intensification of cultivation achieved in this period was probably the introduction of 'convertible husbandry' or the combination of balanced crop and livestock production. Arable land was converted to pasture and back to arable land again through rotation. New nutritious fodder crops were introduced and because this permitted more livestock to be maintained through the winter months, fallows could be reduced since more organic manures could be applied to maintain fertility of soils.

Turnips and clovers mixed with rye grass were valued in the new methods of rotation of crops for cultivating poor soils. New legumes were used for nitrogen fixation. Together with the roots, grass and legumes were introduced as a method of supporting additional livestock, as well as reducing and strengthening bare fallows. This helped both livestock management and arable land quality. A good example is the Nor-folk rotation of wheat-turnip-barely-clover. Over 20% of the total acreage of the country, was affected by the improvements in the eighteenth and nineteenth century.

It must also be noted that the second wave of enclosures was a move by legislation to privatise what was, by custom, land held in common for centuries, to which the entire village had access. Theft of this type of land had of course taken place right from the early sixteenth century carried on by individual acts of terror. The eighteenth century not only legalised this theft but also encouraged it by converting it into absolute private property. Between 1801 and 1831, according to one estimate, 3,511,770 acres of common land had been privatised. The orgy of enclosure and privatisation of common land culminated in the 'clearing of cottages', which literally meant the sweeping off of cottagers living at the edge of the commons. For centuries, legislation had attempted to protect the rights of the same people to eke out an existence, supplemented by the four acres surrounding their cottages. By the 1800s the cottagers were rendered completely homeless by being squeezed out of even this precarious existence. The ranks of the cottagers had been swollen in the preceding 150-odd years by those dispossessed in the first wave of enclosures for pastures. The small farmers and cottagers could by law enclose. However, since fencing was necessary for the enclosure to be considered legal, and the cost of fencing was very high, the poor farmers and cottagers were marginalised, and pressure was put on them by the well-to-do gentry to sell out.

The dispossession of the poor peasant and cottager was completed with the aid of other factors too. The loss of common property rights must have added to the precariousness of their existence. The decline of cottage industries which had played an important role in the lives of the poor as a source of supplementary income would have put further pressure on them. Indebtedness, in the context of a greater use of inputs bought with money, assumed more severe proportions.

The leasing of land was another avenue where the poor and small copyholders and tenants were marginalised. The improvements made in cultivation practices necessitated large outlays of investment. Since the poor tenants could not command adequate investible funds, they were not given leases. However, this preference for richer tenants was often implemented through the forcible commutation of lifetime leases of small tenants. Thus, this period witnessed the completion of the process of dispossession of the vast majority and the formation of the class of wage labour. About one third of the rural population (1,788,000 men and 229,500 women) were hired workers, which was higher than in any other country in that period.

1.10 INVESTMENT, TECHNICAL CHANGE AND PRODUCTIVITY INCREASES—THE AGRICULTURAL REVOLUTION

By the middle of the eighteenth century, land was being cultivated in a manner which was different from that in the preceding 150 odd years. The process of change began between 1650 and 1700. Apart from convertible husbandry discussed earlier, more effective drainage methods improved productivity of claylands and there was an improvement of livestock by cross breeding. Field machines like drills, horse-hoes, cultivators, hay shredders and reapers were adopted in plots which were wide stretches of well drained, levelled and unencumbered land.

Though the initial stimulus for increased productivity can be traced to increased profitability via both cheap wage labour and high price of food accompanied by the export bounty on corn, it ultimately led to an initial decline in prices by the end of

the seventeenth century, and then its stabilisation. This was accompanied, as seen above, by rising output.

The increase in output at lower and stable prices ensured that the major item of consumption for wage earners i.e., food was available cheap. The low price of this wage good implied that the cost of subsistence of wage labour would be low, and hence wages could be kept low without an upward pressure being exerted on them.

Low food prices also implied that the ability of those who bought goods in the domestic market to purchase mass produced industrial goods increased. This increase in their purchasing power helped in the formation of the home market for industrial goods.

Thus we find that at the end of our period of study, coinciding with the beginning of the Industrial Revolution, the process of concentration of property in the hands of a few and the dispossession from any means of production for the majority was complete. This polarisation, and the consequent formation of the reserve army of labour had little to do with natural factors like population growth, or psychological attitudes like thrift or laziness. It was instead an institutional outcome of a complex historical process, the contours of which have been traced above.

Check Your Progress 5

- 1) What was the social and economic impact of the second round of enclosures on the peasantry?

.....
.....
.....
.....
.....
.....
.....
.....
.....
.....

- 2) What were the various measures taken up to increase agricultural productivity in the eighteenth and early nineteenth century?

.....
.....
.....
.....
.....
.....
.....
.....
.....
.....

- 3) How did the Agricultural Revolution contribute to the First Industrial Revolution?

.....
.....
.....
.....
.....
.....
.....
.....
.....
.....

1.11 LET US SUM UP

In this unit you have read about the different stages through which English agriculture passed between the twelfth and the mid-eighteenth century. In this period the classical feudal economy gradually broke down and ultimately culminated in the rise of capitalist relations in English agriculture and the Agricultural Revolution.

The manor was the unit of the classical feudal society. The economic organisation was based on the appropriation of surplus in the form of rent by the landlords from the serfs who, while not owning the land they cultivated, were tied to it for generations. Agricultural productivity was extremely low and it was not simply because of the low level of technology alone. Since the landlords often hiked the rent leaving the serfs with a bare subsistence, the serfs—the peasants and the cottagers—did not have any incentive to undertake measures to increase productivity. In the absence of commercialisation of agriculture i.e., production for the market during early feudalism—the landlords too did not have motivation to increase output. Population also increased at a very slow rate under feudalism—in fact it declined drastically due to the plague epidemic known as the Black Death of 1348.

However, since the thirteenth century, growth of trade and commerce, increase in military warfare, and in size of the feudal aristocracy led to an increased demand for revenue and hence increased feudal exaction. Unable to bear the burden, serfs resorted to illegal flight to the towns. This period also marked a gradual transition from labour rent and kind rent to cash rent. There was also noted a tendency towards differentiation among the peasantry. A well-to-do stratum—comprising the yeomen emerged. These changes altered the tenant-serf relation. The serf became gradually a tenant and could partially benefit from increased productivity.

With the discovery of the New World and the inflow of bullion in the Sixteenth Century, England witnessed a Price Revolution which boosted profits. The wage earners, landlords and the state were losers while the merchants, moneylenders and employers of hired labour benefited from the profit inflation. Landlords retaliated by increasing rent which immiserated the tenants.

Agricultural production became profitable with growing urbanisation and commerce. Landlords took steps to consolidate their holdings and to increase productivity. With the growing demand for wool, thousands of peasants were evicted and cultivable land converted into pastures. These lands were fenced. Hence the term 'enclosure'. Thus 'common' lands became private property, indebtedness and forced sale of land by poor peasants was rampant. Peasants were converted into vagabonds and beggars. The state passed very harsh Anti-Poor Laws to keep wages down and to prevent agricultural labourers to flee from their place of residence and employment thus providing a reserve army of cheap labour to the landlords—hall mark of capitalist development. However, this labour was not 'free' as its mobility and freedom to choose occupation was limited. Simultaneously, the class of well-to-do peasantry—the yeoman—was enriching itself. This class was the one to initiate capitalist development in England's agriculture.

The Seventeenth Century witnessed the Reformation and the Civil War, resulting in a change in the balance of class forces. The feudal elements like the Church, Monarchy and the landed aristocracy lost out to the emerging capitalist forces represented by the landed gentry, yeomen, townsmen, middle men, traders, etc. The New State confiscated a major portion of royalist land, abolished feudal tenures and Court of Wards. However the poor did not benefit to any significant extent. In fact they bore the burden of increased excise taxation. Now, the landed gentry and yeomen were land owners and copyholders were the tenants.

The first wave of enclosures did not immediately create a large reserve of labour for agricultural and industrial capitalists to draw upon. While it accentuated the differentiation among the peasantry, the actual process of creation of free wage labour occurred as a result of the Second Enclosures in the eighteenth and the early nineteenth century. While the First Enclosure was illegal, the Second Enclosure received active state support as by then, the State represented the pro-capitalist

forces. Till 1800, cottagers had managed to eke out a living in the small land they occupied. Now, the laws of the market rendered them completely homeless and destitutes—swelling the rank of reserve army of the unemployed.

The capitalist farmers undertook various measures to increase agricultural productivity. They invested in land and introduced technical changes. All these changes combined were of a dimension of a revolutionary change—change in technology and in relations of production. This agricultural revolution contributed in no small measure to Industrial Revolution.

1.12 KEY WORDS

Conquistadores : Conquerors

Copyholders : Tenants occupying land from the gentry on payment of rent.

Cottagers : Poor tenants living in cottages in the lord's demesne in the manorial set up.

Demesne : Land held by the lord in his manor.

Enclosure : Consolidation and fencing of common lands and lands customarily cultivated by peasants by landlords through forced eviction of tenants. Landlords converted these lands into pastures or cultivated by means of hired labour.

Manor : A self-sufficient economic unit consisting of a village and its surrounding land in medieval and feudal England, operating on the basis of agricultural production and artisanal cottage industry.

Labour rent : Performance of free labour services on the lord's land holding for a specified number of days in a week.

In return the tenant, would cultivate the land belonging to the landlords reap the produce for his personal consumption.

Strip farming : Arable land was divided into long narrow strips. Each strip was the primary unit of cultivation. A peasant would cultivate several strips of varying qualities of land scattered across the village. In the absence of consolidation of land holding, strip farming entailed low productivity.

Three-field System : Plot cultivated in two successive years and left fallow for the third year. In this system for any given year one third of the arable land was not cultivated.

Two-field System : Plot cultivated in one year and left fallow the following year. In this system for any given year half the arable land was not cultivated.

Yeoman : Well-to-do farmer lying in between the poor peasant and the rich gentry in the economic hierarchy.

1.13 SOME USEFUL BOOKS

Deane, Phyllis, 1967. *First Industrial Revolution*, Cambridge University Press, London.

Hill, Christopher, 1968. *Reformation to Industrial Revolution: A Social and Economic History of Britain 1530-1780*. Weidenfeld and Nicholson, London.

Hobsbawn, E.J., 1968. *Industry and Empire*, Penguin Books, London, Chapter 5.

Dobb, Maurice 1963. *Studies in the Development of Capitalism*, Routledge and Kegan Paul, London, Chapters 1, 2 and 6.

Marx, Karl, 1986. *Capital*, Vol. I, Penguin Books, London Chapter 2, 3.

1.14 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Changes in the Agrarian
Structure : Classical
Serfdom to Second
Enclosure

Check Your Progress 1

- 1) Read Section 1.1 and answer
- 2) Read Section 1.2 and answer
- 3) Read Section 1.3 and answer

Check Your Progress 2

- 1) Read Section 1.4 and answer
- 2) Read Sub-section 1.4.4 and answer
- 3) Read Sub-sections 1.4.2 and 1.4.3 and answer

Check Your Progress 3

- 1) Read Section 1.5 and answer
- 2) Read Sub-sections 1.6.1 and 1.6.2 and answer
- 3) Read Sub-section 1.6.3 and answer

Check Your Progress 4

- 1) Read Section 1.7 and answer
- 2) Read Section 1.8 and answer

Check Your Progress 5

- 1) Read Section 1.9 and answer
- 2) Read Sections 1.9 and 1.10 and answer
- 3) Read Section 1.10 and answer.

ignou
THE PEOPLE'S
UNIVERSITY

UNIT 2 INDUSTRIAL REVOLUTION

Structure

- 2.0 Objectives
- 2.1 Introduction
- 2.2 Prelude to Industrial Revolution
 - 2.2.1 The Domestic Market
 - 2.2.2 The Export Market and External Sources of Raw Materials
- 2.3 State Policies and Mercantilism
 - 2.3.1 The Rule of Protectionism, 1649-1846
 - 2.3.2 Trilateral Trade Patterns and Contribution to Capital Formation
 - 2.3.3 Institutional Aspects of the Society
- 2.4 Industrial Revolution
 - 2.4.1 Industrial Capitalism
 - 2.4.2 The Cotton Industry—Origins
 - 2.4.3 The Cotton Industry—Technical Innovations and Expansion
 - 2.4.4 Other Factors Behind the Rise of Cotton Industry
 - 2.4.5 The Iron Industry
- 2.5 Government and the Industrial Revolution
- 2.6 Human Results of the Industrial Revolution
- 2.7 Let Us Sum Up
- 2.8 Key Words
- 2.9 Some Useful Books
- 2.10 Answers/Hints to Check Your Progress Exercises

2.0 OBJECTIVES

This unit will give you an idea of :

- the conditions in pre-Industrial England that were conducive to Industrial Revolution
- the main features of the Industrial Revolution
- the relation between commercial policies and rapid growth during the Industrial Revolution.

2.1 INTRODUCTION

The period which we are going to study, that between 1760 and 1840, is generally described as the period of the Industrial Revolution. The term was coined by Jerome Adolphe Blanqui in 1837, but the credit for the general currency it has been enjoying for more than a century must go to Arnold Toynbee. It was his "Lectures on the Industrial Revolution" (1884) that firmly affixed the words 'Industrial Revolution' to the events in the British social and economic experience of those years. A revolution implies change and the period under discussion saw significant changes in many aspects of British life. To the contemporaries, Blanqui and Toynbee for example, the changes seemed dramatic. To us, made blasé by the knowledge and experience of many other revolutions since then the British history of those years might seem less startling. But it is unlikely to be entirely unimpressive, and no amount of de-dramatisation, thought by many as an inevitable product of the 'march of time' can take away the following attributes of the Industrial Revolution: it was the first, in some ways classic and for some time the only example of industrialisation. Little wonder then that the Industrial Revolution has been one of the most frequently and extensively studied periods. Not every one among its students were favourably disposed towards the results of the Industrial Revolution, but few failed to notice its pivotal role in influencing British and Western economic and social life. To the Industrial revolution goes the 'credit' for laying the foundations of one of the most influential socio-economic systems of our time, industrial capitalism. To it also goes

the distinction of providing the material for the most effective and influential critique of that system, Karl Marx's critique of industrial capitalism.

The period of the Industrial Revolution was not only one of accelerating industrial and economic growth but also of social and economic transformation. The foundation for such quantitative and qualitative changes was neither built suddenly nor isolated; it built up over time and was spread across many factors. We now turn to examine these factors, which can be described as the preconditions for the Industrial Revolution.

2.2 PRELUDE TO INDUSTRIAL REVOLUTION

The story of British Industrialisation is one of capitalist industrialisation i.e. industrial expansion was carried out in a system where the industrial population was divided into a relatively small group of owners of the means of production, the capitalists and a larger group of workers who sold their labour power (i.e. capacity to work) to their capitalist employers in return for wages. The capitalists' aim is to make a profit. Production is organised with this primary aim and most of the decisions regarding the production process is subordinated to this aim. The industrial Revolution, as we have noted, was a period of great transformation. The fact that private pursuit of profit by numerous capitalists led to such a transformation implies that certain conditions existed in Britain, which made profit making through production a viable activity. Few things are more important for sustained generation of profits than markets. The major precondition for the Industrial Revolution was the existence of markets for British products. Linked to this economic precondition is a political one, the existence of a government which puts its considerable and numerous powers firmly at the disposal of the business of profit making. Also important are certain institutional arrangements and social and economic features, most of them being products of gradual change over centuries, which provided Britain with a congenial framework for the expansion of private enterprise led industrialism. We will now discuss each of these preconditions in turn.

Both export market and domestic markets were important in the genesis of the Industrial Revolution. They played different roles in creating the conditions for industrialisation: the domestic market was larger and more stable while the export market was the more dynamic if more fluctuating component.

2.2.1 The Domestic Market

Population growth was not a major source of domestic purchasing power in Britain during the pre-industrial days. Population as an issue of scholarly inquiry has raised many difficult questions and protracted disputes but there is near unanimity over the proposition that the significant growth in population came with the Industrial Revolution not before it. The home market in the immediate pre-industrial decades was a result of long periods of economic growth which had created rising incomes, especially in the first half of the eighteenth century. It was also bolstered by the fact that during this time the composition of population changed in the favour of younger adults and against children (this change typically creates more demand for products which are not necessities). The specific and the most important effect of the home market was felt in three sectors: transport, food and coal.

The existence of a nationwide market for many of Britain's manufactured products necessitated the creation of cheap and reliable means of transport. In a country crisscrossed by numerous waterways, it was not surprising that river and canal transport were to undergo the most important improvements. However roads too were not left out of this 'transport revolution'. Canals cut the cost of transport by as much as eighty per cent.

This well developed transport system created during the pre-Industrial Revolution days meant that British Industrialisation when it came did not have to face the problem which bedevilled many later efforts: the problem of an adequate transport system.

The home market also boosted the demand for coal, which later became a major component of the expansion in capital goods industries. The increasing urbanisation gave coal its market and well before the revolution its production were already in millions of tonnes. When it was called upon to play a pivotal role in the age of the railways and iron and steel, the coal producing sectors comfortably rose to the occasion. That it did so was in no small way because of the sound base created during the pre-industrial years.

A large home market also meant substantial demand for food (and drinks), especially with urbanisation. Food and beverages in early eighteenth century Britain were the industries where the application of mechanical and engineering knowledge was pioneered. While they did not transform the economy, they created important examples: none more ubiquitous and easily (also perhaps fondly) remembered than the beer handle, whose application vastly improved the efficiency with which the thirst of the patrons of Britains' proliferating public houses could be met.

The home market had another important role, that of creating the basis for a **generalised** industrialisation. In its size and stability lay the assurance that the process of industrial expansion once started would not fizzle out. Thus, even though the Industrial Revolution was primarily a one sector led transformation (cotton textiles, as we shall see later) its import and message was effectively passed through the already existing market of national dimension. Furthermore the domestic market also provided the safely valve against the sudden disappearance of export markets, which tended to coincide with wars and upheavals.

2.2.2 The Export Market and External Sources of Raw Materials

The export market, in contrast to the home market provided the spark and the dynamism required for a radical transformation like the Industrial Revolution.

Table 2.1 : Percentage increase in home market and export market

<i>Period</i>	<i>Home Market</i>	<i>Export Market</i>
1700-1750	7	76
1750-1770	7	80

It was this phenomenal increase in export markets that ignited the fuse of industrial expansion. Cotton textiles, the prima donna of the Industrial Revolution was largely dependent on exports. Moreover, raw cotton was a raw material which could not be grown in European climatic conditions and was entirely imported. Trade effected substantial improvements in sea transport which inturn stimulated a whole range of practical innovations and a number of practical men, with an eye for the profits; many of these groups were to later be important components of the Industrial Revolution. It is certainly not entirely accidental that Henry Cort, who brought about great changes in iron manufacturing, started his professional life as a naval agent.

What led to such mammoth increase in the export market and external access to raw materials for British products? For the developing economies of today, many of whom are trying to follow an export led model of development, the answer will be of little help. For despite the economic superiority and internal dynamism which Britain possessed then, the principal reason why export markets could be secured and maintained was not due the application of the harmless doctrine of comparative advantage, but the relatively more eventful and ruthless doctrine of war and colonisation. War helped to snatch away the export markets of competitors and colonisation was a wonderfully effective way of obtaining valuable raw materials and of destroying internal competition in manufactures within particular countries. In the more lax standards of international conduct which prevailed in those days, Britain was not the only country to have the ability to practise such aggressive internationalism. But it certainly was the only one with the determined and fully committed political will to put this doctrine into practice. This point brings us to the role of the government, to which we now turn.

1) What are the preconditions for an Industrial Revolution through capitalist path?

.....
.....
.....
.....
.....
.....
.....
.....

2) What determines the size of the domestic market?

.....
.....
.....
.....
.....
.....
.....

3) What led to a dramatic increase in the export market for British products?

.....
.....
.....
.....
.....
.....
.....

2.3 STATE POLICIES AND MERCANTILISM

International policy in eighteenth century Britain was completely dominated by economic priorities. Governments were ready to wage war for the interest of domestic industry. Britain's dominance in this respect is to be attributed largely to the fact that more than a century before France's famous Revolution of 1789, England had overthrown the feudal political order during the Civil War of 1640-1660 and embarked on a nationalist and expansionist policy. To this end British Navy was transformed into the greatest naval force in the world. The might of the imperial navy which had the blessings of the government on its head and the interests of British trade and commerce in its heart helped create the biggest and the most secure source of valuable food and raw materials and the largest export market any country in the world has ever known. On the national plane the British ruling groups were more amenable to and later on increasingly indistinguishable from manufacturing interests, in contrast to commercial and financial ones. British governments also effectively produced some of the important conditions of capitalist industrialisation: it protected private property and maintained internal law and order. Also in the early years of industrialism it was not always unduly moved by the plight of the not so fortunate participants in the revolution and thus did not interfere in the process of private pursuit of profit by those who had the means and the inclination to do so.

2.3.1 The Rule of Protectionism, 1649-1846

One of the commonly held misconceptions regarding the Industrial Revolution and the rise of large scale capitalist manufacturing production is that it was associated

with 'free trade'. On the contrary in reality a very prolonged period of intense protectionism marked the adolescence, flowering, and maturity of industrial capitalism in England. This period of protectionism started with the victory of the capitalists in the Cromwellian Civil War in 1649 and ended only in 1846, nearly 200 years later, long after the capitalist system was firmly established.

The mercantilist theory of the 17th century envisaged the addition to the wealth and well-being of a country in terms of a combination of increasing the export surplus from the country and keeping the terms of trade (ratio of export prices to import prices) in favour of the country. Now normally if export prices are raised to benefit the exporting country, importers in other countries might reduce their demand and hence net export earnings might fall if demand is price elastic. The Mercantilists however did not consider this a problem because the country to which goods were exported was brought under coercive colonial domination and had no choice in the matter of demand.

The Mercantilist policies were executed through a combination of colonisation by armed force and legal decree. Ireland was the nearest colony which was conquered by England, its land divided into large estates among English landowners with the Irish reduced to tenants. Ireland was forbidden to export meat, wool and butter. These prohibitions were enforced by a strict naval blockade.

The Navigation Act of 1651, amended in 1655, laid down that all English colonies were to be subordinated to Parliament and that all trade was to be monopolised by English ships. Thus a coherent national imperialist policy was formulated in England before any other country.

The North American colonies were forbidden to manufacture a single item which might compete with British exports, ranging from hats and pins to textiles and iron manufactures by a series of Act from 1691. They had to import all these items from England as well as pay for the freight of English-owned ships. Similarly manufacture was forbidden in the Caribbean colonies and every item of clothing as well as the chains and shackles used on the slaves had to be compulsorily imported there from England. Although raw sugar was produced in Jamaica the refining was done in Bristol.

Within England there were a series of Acts protecting British manufactures against the competition of cheaper foreign goods while allowing the free entry of raw materials necessary for manufacturing. Thus when the activities of the East India Company in importing calicoes and fine printed textiles from India and Persia, created a growing demand within England, the wool industry fearing a loss of part of its market by substitution of cotton for wool, demanded and obtained from Parliament in 1700 an absolute ban on use of these textiles within England. Smuggling continued and there was another very strict Act in 1721 which imposed heavy fines on individuals found wearing Indian cottons and on merchants found to be dealing in imported cottons. This prohibition had an important effect in later stimulating import substitution through the growth of an English Cotton Textiles industry which symbolised Industrial Revolution, (as we will see in Section 2.4).

It is clear that these policies had a consistent aim, of encouraging manufacturing within England by every means possible, and in colonies of destroying any existing manufacturing industry or making it impossible for a new industry to come up, in order to ensure a ready market for British exports which had to be compulsorily absorbed by the colony.

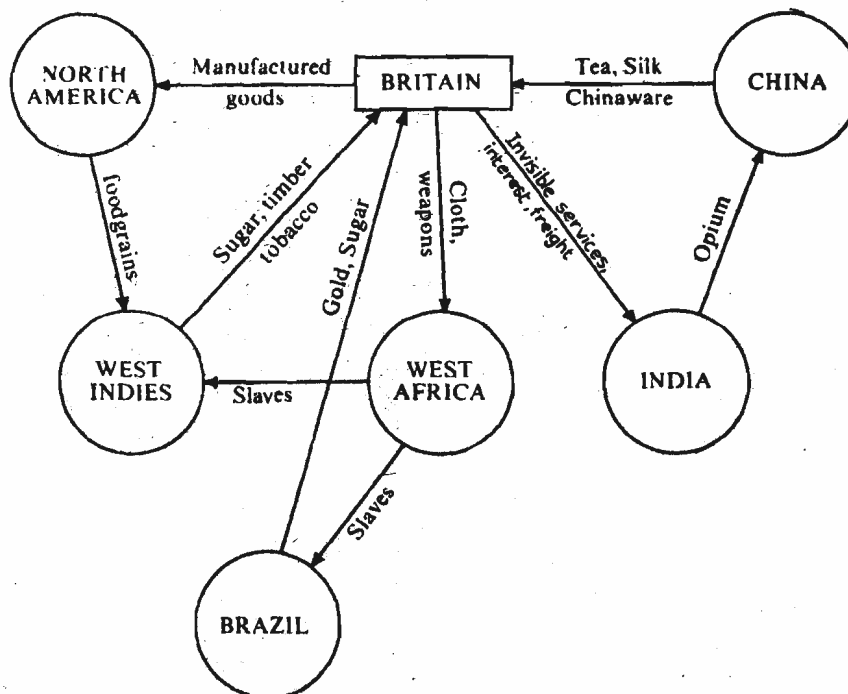
Where colonies were settled by emigrating English and other Europeans, they eventually revolted and acquired Independence, as for example the N. American colonies which fought their War of Independence against England in 1776. The tropical colonies however in Asia and the West Indians remained subjugated until the middle of the 20th century. Over this long period they were forbidden to protect their own manufacturing in any way while being made captive markets for British exports. The third quarter of the 18th centuries was certainly marked by a demand for 'free trade' by the manufacturing capitalists in Britain and their theorists such as David Ricardo and Adam Smith, but that demand had to do with freedom to import foodgrains, (which had been restricted by the landlords who wished to maintain high

food prices within the country to maximise their own gains) and therefore concerned abolition of the Corn Laws restricting corn imports. This demand for free trade had nothing to do with abolishing protection to English manufacturing. Varieties of machine made English cloth continued to be protected by high tariffs against Indian handloom cloth upto as late as 1846 when tariffs were done away with finally because Britain no longer needed them.

2.3.2 Trilateral Trade Patterns and Contribution to Capital Formation

The consumption pattern of ordinary people in Northern Europe before the European domination of world trade, was restricted to a rather narrow range of locally produced goods. The cold climate and short growing season permitted only one crop and a restricted range of fruit and vegetables, whose supply ceased completely during winter. Clothing was mainly of leather and wool. By the early 19th century however the consumption pattern had become highly diversified and balanced owing to the inclusion of a large range of tropical goods used for eating, drinking, wearing or building furniture, housing and other durables—such as tea, coffee, cocoa, cane sugar, rum, mahogany, teak, raw cotton for textiles, indigo, jute, citrus fruits, tropical vegetables and fruits, spices, tobacco, rubber, and various minerals among others. None of these are producible within Europe (except citrus fruits in a restricted region on S. Europe). The high dependence of European (and N. American) living standards on import of tropical goods continues to this day.

In the 17th and 18th centuries Europe had nothing much to offer to the ancient civilisations like India or China to balance the growing imports of tropical goods which had a potentially large and elastic demand. These imports had to be paid for in bullion (precious metals) and this fact itself restricted the trade. The solution was sought through acquisition of political control over the tropical territories, and either direct production through imported slave labour of the valuable commodities (as in the W. Indies) or acquisition of those commodities from existing producers by taxing them as in India. Thus, the English East India Company's problem of balancing the trade with India was 'solved' when in 1765 Clive acquired the Diwani of Bengal. For the land revenue collected from the peasants could then be used to purchase Indian goods for export to England. Moreover these goods, obtained 'free' (as the commodity—equivalent of tax) could be re-exported to other European countries (where they were in great demand) to pay for English imports of strategic goods like Swedish bar iron, timber, pitch and tar for the Navy. After 1765 England's trade with Asia grew very rapidly owing to colonisation, and between 30 to 35 per cent of all tropical imports were re-exported to other countries, 80 per cent of re-exports going to Europe to pay for imports from there.



Note : The opium triangle with India and China developed to a maximum during a later period, 1820-1870, compared to the triangular trade with W. Africa and various parts of America which flourished throughout the 18th century.

The control over territories and Mercantilism permitted England to follow highly flexible patterns of triangular balancing of trade. This means that if England wished to acquire goods from a sovereign country A but country A had no reciprocal demand for English goods, England would then use the products of its colony C to pay for its own net imports from A, while not having to pay anything herself to colony C since taxation in the colony financed purchase of exportables from C. Such a triangular pattern was the India-China-Britain opium triangle. Britain had a large trade deficit with China (which it did not control politically in the sense of imposing taxes). It therefore expanded the production of opium in India and forced China to import the opium after prosecuting the opium wars in 1842-44 which opened the Chinese ports. Exports of Indian opium paid for England's trade deficit with China, but this Indian opium, being purchased out of Indian tax revenue did not involve any obligation on England vis-a-vis India, to supply an equivalent value of goods. (The yarn and cloth which India was obliged to import from U.K. from 1813 had to be paid for by Indian exports of goods to U.K.).

Another trade triangle was the W. Africa-W. Indies-England slave triangle. Arab Slave traders kidnapped W. Africans from their hinterland village communities and sold them to the English at the ports in exchange for weapons and cloth. The slaves were transported in English ships to the Caribbean (also to Brazil, and the southern part of N.America) under conditions so inhuman that many died, and sold at five to six times the purchase price to English plantation owners. There they were given a bare subsistence and set to work to produce sugar, tobacco, cotton and other commodities which were then imported into England partly for internal consumption and partly for re-export.

The profits from these trading patterns (each involving at least one element of costless acquisition), were very high and they formed the bedrock of the rise of large urban centres like Liverpool and Bristol, led to the establishment of a range of industries in England from sugar refining, rum distilling and shipping to the manufacture of leg irons, handcuffs and shackles for the hapless slaves, and the establishment with slaving profits of famous banking houses like Barclays. Adam Smith who is generally regarded as the theoretician of free trade and laissezfaire, described the slave trade in his *Wealth of Nations*, as one which 'raised the Mercantilist system to a pinnacle of glory'. Smith was not opposed to the slave trade or to Mercantilism in the 17th and early 18th Century, but thought that with ongoing Industrial Revolution the need for those policies was over and unrestricted trade was best suited to new conditions.

In Unit 15, we will study in more detail the difficult question of what was the magnitude of one-way (unilateral) transfer from the tropical colonies to England during the Industrial Revolution. Here we may simply briefly note that the magnitude was in fact quite substantial; for England was a small country then with hardly 10 million population, which through aggressive commercial wars and colonisation had acquired control over ten times more populous and resource-wise much richer territories. A pioneering estimate by S. Habib of the percentage of combined transfers from Asia and W. Indies to the British gross national product puts it at 4.8 per cent in 1801, which constituted as much as 70 per cent of estimated British domestic capital formation at that date.

We have already studied the way in which the enclosures within England had helped to create one essential prerequisite, the labour-force required for expanding industry. Another prerequisite of the rise of industrial capitalism is the prior accumulation of capital in the hands of people able and willing to put it to profitable use in production employing hired labour. This 'prior' or 'primary' accumulation was greatly aided by the network of monopoly trading and shipping rights which we have described above, which yielded fabulous profits over many decades.

2.3.3 Institutional Aspects of the Society

Britain was the first country where feudalism broke down and capitalism, with its

division of the economic population into property owners and workers, developed. In contrast to other European countries where serfdom also disintegrated, in Britain there was enough concentration of land in the hands of a group of land owners which perverted the strengthening of a body of free peasants. Thus in Britain capitalist agriculture could flower relatively early and not be hindered by state power using the peasants as a bulwark against agrarian capitalism. The spirit of economic individualism, the hall mark of Industrial entrepreneurs had been present in England perhaps as early as the 12th and 13th centuries and had developed to the extent by the mid 18th century, that making money from trade and industry was seen by people who were influential in matters of state, to be a perfectly legitimate and desirable action.

By the 1750s Britain was also a relatively well developed economy, ready to take the forward leap of industrialism. It had a flourishing traditional manufacturing industry supplying to a national market and a growing economy. There was little shortage of capital, relative or absolute and a growing band of theorists for the free market system, the most notable being Adam Smith. The notion that private pursuit of happiness also resulted if left unhindered by such clumsy interventionists as the State, in social good was an attractive one for capitalism. The Smithian 'invisible hand' (and later the Ricardian 'Iron law of wages') were used by many propagandists and practitioners of the profit-motive to bolster the case for capitalism. In the early years of the industrial revolution, when the privations of large masses of the population were great, such intellectual tools could be used (and misused) to try and placate both one's conscience and one's less fortunate compatriots (though the latter was done with noticeably less success than the former).

Check Your Progress 2

- 1) Was Britain's Industrial Revolution associated with 'free trade'? Discuss.

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

- 2) How did the pattern of trade of Britain with tropical countries change after their colonisation by the former?

.....

.....

.....

.....

.....

.....

.....

.....

.....

- 3) Explain the concept of triangular pattern of trade. How did Britain benefit from this kind of trade?

.....

The typical production unit in industrial capitalism was the factory. The factory was a combination of specialised human labour with specialised machines. It gave rise to a new rhythm of work, where the pace set by the engine was continuous and inhuman; and where the extent to which the individual worker needed to use her strength and intelligence was considerably reduced. It also subjected the workers to the unrelenting discipline of mechanisation. In the telling phrase of Marx, "in manufacture and handicrafts, the worker uses a tool; in the factory he serves the machine."

In a later section we shall see the social consequences of these new forms of society and organisation of work. The remaining part of this section is devoted to the study of the two principal industries of the Industrial Revolution, cotton and iron.

2.4.2 The Cotton Industry—Origins

Cotton was by far the most important industry in this period of British industrialisation. For a major part of this period fluctuations in British industrial growth and balance of payments were tied to the cotton industry. The quarter century following the battle of Waterloo, saw the zenith of cotton industry; it was also the boom years for British industrialisation. When cotton plummeted to a 0.7% growth rate in the last quarter of 19th century, so did industrial growth rate.

Table 2.2 : Percentage growth rate of Industrial Production : ten year periods

Year	Growth Rate	Year	Growth Rate
1800-10	22.9	1850-60	27.8
1810-20	38.6	1860-70	33.2
1820-30	47.2	1870-80	20.8
1830-40	37.4	1880-90	17.4
1840-50	39.3		

Let us briefly look at the origins of this industry before considering the reasons for growth. The fact that it was cotton textiles which was the fastest expanding 'leading sector' of the Industrial Revolution in Britain is surprising at first sight for at least two reasons: firstly woollen textiles, not cotton, was the traditional manufacturing industry catering to mass demand in England for centuries, with skilled workers as compared to no tradition of skills to speak of in working with cotton. Secondly, raw cotton cannot be grown in Britain or indeed in most of Europe at all and had to be entirely imported into Britain.

It is not possible to understand why despite this it was cotton and not woollen textiles which was associated with fast-growing factory production, unless we refer to the activities of the East India Company. It was the import into England of the calicoes and muslins, the printed and painted textiles from Asia (mainly India but also Persia) which created a growing demand within England for these fabrics. They were used for furnishing, curtains and clothing and became fashionable with both the aristocracy and gentry and popular with ordinary people owing to their comfort in wear and washability compared to woollen fabrics. The nearest rival made in England to the fabrics imported from India was *fustian*, a very coarse cloth made from a mixture of domestically grown flax fibre (linen) and thread from imported cotton.

We have already seen that the powerful woollen industry had demanded, and obtained a ban on the use of Indian and Persian fabrics, in order to keep a monopoly of the cloth market in Britain. But ultimately this ban of 1700 and 1721 had precisely the effect of stimulating import substitution and the growth of a domestic cotton industry protected from Indian imports. For as long as there was a pent-up, unsatisfied demand for the banned cotton fabrics within England, anyone who could imitate those Indian fabrics had the prospect of making a great deal of profit from the large potential market which already existed. In short, the potential profitability of domestic cotton cloth production was raised greatly by the banning of India imports.

Table 2.3 : Cotton in the Industrial Revolution

A. Imports Raw Cotton. (By volume)	
(1780 = 100)	
1770	60
1780	100
1800	800
B. Exports of Cotton Textiles. (% of total British home produced)	
1760	18
1815	40
1830	52
C. Exports of Cotton Textiles (By volume). (1760 = 100)	
1760	100
1780	350 (approx.)
1810	3500
1830	10500
D. Percentage of National Income accounted by Cotton	
1802	4 to 5%
1812	7 to 8%
1830	7 to 8%
E. Prices of Cotton Yarn (per lb.)	
1786-87	38s.
1800	10s.
1807	6s.9d.
1832	11 1/4d.

Sources : Phyllis Deane and B.R. Mitchell: *Abstracts of British Historical Statistics*. (1962). Eric Hobsbawm: *Industry & Empire*. (1968). Karl Marx: *Capital*, Volume I (1928).

The problem for the English however was that although they could import raw cotton, there was no centuries old tradition of spinning and weaving cotton such as Asia had. The fineness and strength of the thread spun with crude spindles and the colour and variety of design of the fabrics woven on simple looms by Indian artisans, could not be matched despite their best efforts, by English artisans, whose product was very poor in quality. Where human artisan skills are deficient, mechanical skills are sought to be substituted. This is the underlying reason for the relentless search, under the goad of the prospect of high profit, of mechanical means of substituting for missing human skills in cotton textile production in England. Of course, if a certain minimum level of mechanical skills had not already developed, such a search would have been perhaps fruitless.

It so happened however that the long maritime tradition in England had fostered mechanical skills to a high degree. Instruments for measuring latitude, for determining the position of ships at sea from astronomical observation, and for determining balance, had to be developed. Artisans familiar with clockwork mechanisms and cabinet makers were some of the people who pioneered the first mechanical innovations in weaving and spinning cotton. It was these mechanical innovations which permitted at last after 30 years of effort thread to be produced which had both fineness and strength and fabrics to be woven at lower cost than that produced by the handloom weaver of Asia. (Nevertheless specific finer varieties of Indian fabrics faced high tariffs in England as late as the 1830s).

2.4.3 The Cotton Industry: Technical Innovations and Expansion

There is a certain dialectical (to-and-fro) movement observable in the sequence of innovations in cotton textile production. The inability of weavers to rapidly absorb even the little yarn produced by the first clumsy efforts of the spinners in England, led to the invention of the 'flying shuttle' by Kay in 1733 in which the shuttle was mechanically thrown from one end of the loom to the other. This both speeded up weaving and also freed the maximum width to which cloth could be woven, from the arbitrary limitation of the length of the weaver's arms. Now the spinners could not keep pace, and methods of speeding up spinning as well as improving the quality of hand-spun yarn (which was very coarse and weak compared to Asian yarn) became necessary.

After a number of abortive efforts (by Wyatt and Paul among others) Hargreaves finally, over 30 years later in 1765, succeeded in producing a mechanical spinning device which he called a 'jenny'. This had eight spindles which could be set in motion at the same time by one worker and spun a tolerably fine thread. Jennies got progressively bigger and in Hargreaves' own lifetime jennies with upto 80 spindles each were being used. But the thread still broke easily, and subsequent modifications were concerned with giving a twist to the thread to increase its strength. Arkwright's water-frame substituted water-power for the human hand in operating the spindles while Crompton's 'mule' (a cross between the jenny and water-frame) finally produced a thread which was both fine and strong. The mule spindle reigned supreme for over a century after its invention.

These mechanical devices, though simple wooden ones using little iron, were nevertheless too expensive to be owned by individual artisans. Their widespread adoption in production was accompanied by a) an enlargement of the scale of operation, with small workshops and manufactories giving way to larger ones where the capitalist supervised workers operating dozens of machines; b) it also saw a shifting location of the factories as the motive power changed from the human hand to the force of running water to finally the application of steampower. The small-scale dispersed nature of traditional production gave way first to concentration of factories near fast-flowing streams, with the widespread adoption of the water-frame. Indeed the term 'mill' for factory still survives from the time that water-power was used. Finally the location shifted to near the northern English port of Lancashire where a combination of damp climate and easy access to imported cotton favoured the industry.

These simple mechanical innovations raised labour-productivity tremendously. With a 80 spindle jenny a single worker could spin 80 times more thread than, say, an Asian spinner working with the traditional spinning-wheel. The unit cost of production of yarn, and therefore of cloth, fell drastically. Every such labour-displacing innovation was at first bitterly opposed by the spinners, who attacked the inventors and broke the machines, fearing unemployment. But the very rapid expansion of the market ultimately led to an increase in employment—first the domestic demand was saturated, then English machine-made yarn and cloth displaced imports from Asia by Europe and other countries, and finally invaded the Asian market itself.

2.4.4 Other Factors Behind the Rise of Cotton Industry

Several additional factors help to explain the rise of the cotton industry. Colonial economic links, forged aggressively over the years, provided both the source of cheap raw material and vast export markets. In the peak of the cotton industry's growth, during 1830s, raw cotton made up to 20% of all net imports and cotton exports accounted for over half the value of total exports. For raw materials it relied on the plantations of Africa and later those of Southern USA. For markets it had the free run of the markets of Africa and when the East India Company lost its hold over the policy makers the markets of India and the far East. The success of cotton also depended upon the fact that it was a consumer item, with a ready demand (requiring no prior industrialisation or radical change in taste) and made relatively easy demands on the factors of production in the British economy. It was labour (women's and children's labour) intensive and required capital investments within the reach of the economy.

But by far the single most important domestic factor which explains the prodigious growth of the industry is the extremely favourable position in which the capitalist employer operated in this period. The Industrial Revolution has been described as the result of unplanned activities of small manufacturers. These men for their success depended on this ability to respond to economic opportunities without any hindrance and to shift the pains of adjustment to others. They were given ample space to do both of these in this period. The work force predominantly comprised women and children who were mostly unskilled and unorganised. The employer could hire and fire and change the working time at will. Factory workers then worked upto 16 hours a day for subsistence wages. Handloom weavers, as their situation got desperate worked for longer hours and lesser returns. Wage rise always remained

below output rise and even when the export prices fell profits were maintained. It is this ability of the employer to extract high rates of profit which enabled the manufacturers to plough back a large proportion of their earnings into more investment. This not only created economies of scale but also increased the efficiency by replacing older machines with new ones. Had this sustained profit level not been maintained private investors would not have risked their capital in large scale factory production. High levels of profit gave cotton industry the cloak of business respectability and helped attract ambitious men. These together with the pliant workforce and markets make up the story of the first sector to undergo modern industrialisation.

Cotton definitely set the striking example of large scale factory production to other industries. It also stimulated the chemical and engineering industries. The cotton factories were the first examples of the new 'iron-frame' construction and adoption of gas lighting. Counterbalancing these is the fact that cotton did little to stimulate directly the strategic sectors of any industrialisation: capital goods, in this case coal, iron and steel. It was certainly the most prominent and fastgrowing industry of the industrial revolution. But the development of other industries during this period and later had little to do directly with the development of the cotton industry, other than through the redirection of profits made in the latter.

2.4.5 The Iron Industry

Unlike cotton, large parts of the iron industry were already operating on capitalistic lines before the Industrial Revolution. The industry itself was relatively small and the demand was mainly from shipbuilding, munitions and related activities. It was only with the industrialisation of Britain and other countries that the industry saw a steady expansion of domestic and export markets. It was with the coming of the railways in mid-19th century that the industry saw a real quantum leap in production.

While the industry was waiting to come into its own, a series of innovations helped raise the capacity. The important ones among them were: replacing of charcoal with coke from iron smelting purposes, the invention of puddling and rolling and Nielsen's hot blast. The first meant the freedom from the dwindling supply of one kind of fuel, charcoal and the switch to a more abundant and less fragile (hence easily transportable) fuel source, coke. The second, invented by Henry Cort, enabled the large scale production of bar iron with coal fuel and also the production of quality wrought iron. The third involved the heating of the air used in the blast which resulted in much lower coke consumption and substantially increased output.

Iron, unlike cotton, is a producers' good and has both backward linkages (i.e. linkages with those sectors which supply the industry) and forward linkages (i.e. linkages with those sectors which the industry supplies). Iron created demands for **British** raw materials like coal, iron ore and limestone. These inturn generated a demand for the transport industry, especially those of canals. On the supply side it produced one of the most vital raw materials for industrialised economies at a cheap rate. Continuing industrialisation required that iron amongst other things, be supplied inexpensively and abundantly. The second phase of British industrialisation owes its success to a large extent to the progresses made in the iron industry during the Industrial Revolution.

Check Your Progress 3

1) Why is Industrial Revolution a revolution?

.....

.....

.....

.....

.....

.....

.....

.....
.....
2) What is Capitalism? What is Industrial Capitalism?

.....
.....
.....
.....
.....

3) How did the cotton industry play a leading role in Britain's industrialisation?

.....
.....
.....
.....
.....
.....
.....
.....

4) What role did innovations play in the development of the cotton textiles and the iron industry?

.....
.....
.....
.....
.....
.....
.....
.....
.....

2.5 GOVERNMENT AND THE INDUSTRIAL REVOLUTION

The *'laissez faire'* view of the role of government saw it as one of non-interference with the functioning of the free enterprise market system. Beyond creating the political conditions of suitable rights and laws and abolishing hindrances to free pursuit of profit and free trade the government, it is argued, did little to help the Industrial Revolution. This view has been turned into an article of faith by many commentators. But the real character of the role of the government was quite different, certainly much more complex than the simple hands-off role described by the above view.

Firstly, as we have already noted, it actively created the conditions in which British products could find markets i.e. through war and colonization. Once the market was secured and then maintained by the strong arm of gunboat diplomacy it was easy to preach the virtues of free trade. Selective amnesia prevented many observers from noting that it really was, in the words of Rajni P. Dutt, 'one-way' free trade. Secondly the government in the form of 'Poor Laws' promoted, or thought it was promoting (for in some cases the reasonings were wrong) capitalist industrialisation. It made the 'Poor Law' (the law governing the provisions to be made for the

destitutes) as cheap as possible, to force the poor into the labour market and discourage the growth of population (which it was argued leads to general impoverishment). That the arguments were far from sound and the effect of the Poor Law to produce cheap labour far from certain do not detract from the fact that this was the example of the government trying to influence social parameters so as to achieve the goal of industrialisation. A similar role was played by the numerous laws enacted to foster discipline amongst 'errant workers' and vagrants. These were examples of active involvement in trying to create a pliant and disciplined work-force necessary for the harsh years of early industrialisation.

Thus any evaluation of the role of government in Industrial Revolution must take into account its active part in fostering capitalist development. Private pursuit of profit was the chief force behind this development but it could not have done what it did without the willing and the visible hand of the government. The latter did not interfere in the profit making of capitalists, but it made sure that territories and peoples not willing to fall in line did so, sometimes with the might of the sword, at other times through the power of its laws.

2.6 HUMAN RESULTS OF THE INDUSTRIAL REVOLUTION

As it should be expected the Industrial Revolution affected different groups in different ways. The gentry and the aristocracy did well, with the rents increasing on the lands they owned (due to larger demands of agricultural produce and the mines and railways which passed through their lands). Their social standing remained unimpaired. The more affluent among the rising group of industrialists were absorbed within the nobility. A great majority of this new group however formed the bedrock of the new 'middle class'. They were politically vocal and increasingly well represented and drew their intellectual inspiration from the doctrines of liberal economics, which not surprisingly flowered during this period. The greatest disorganisation, indeed, disruption happened in the lives of the workers. They were now dependent only on wages for their livelihood. They had to adjust, often under pressure and always with difficulty to the regularity and the monotony of industrial work. Their lives were for the most part spent in the Dickensian Squalors of the new cities which produced frequent epidemics. It was not until well into the 19th century that some recognition was given to the grotesquely unequal position of workers in the new system and legislations made to lessen their privation. The waves of protest and discontent which was witnessed during this period was an expression of the desperate dissatisfaction of the majority of the people with the new way of life. For them the Industrial Revolution had taken away the moorings of the old ways and given precious little in exchange. We can do no better to understand this than to quote from a contemporary observer, "wretched, defrauded, oppressed, crushed human beings lying in bleeding fragments all over the face of the society." The first army of industrial workers unsurprisingly found the first Industrial Revolution callously unmindful of their needs.

That the industrial revolution led on to another and more comprehensive phase of industrialisation is a fact. To many contemporary observers, robbed of the benefits of hindsight, such a profusion seemed far from inevitable.

The poverty of the masses placed a limit on the expansion of home markets and when the fast pace of industrial production had saturated the vast colonial markets, industry faced a demand crisis. The most eloquent testimony of this is in the fact that the only notable exporter of industrial goods, Britain, was unable to maintain an export surplus in the 1830s and 1840s. Profits rates fell too, even in colonies. Tragically the prevalent economic orthodoxy did little to help the situation. With its insistence on the maximum possible diversions of incomes to profits and the law of subsistence wages the benefits of higher wages, in form of higher mass demand and higher productivity were overlooked. The workers had not enough to eat and the industrialists not enough profits to justify reinvestment. The deep discontent this

vicious circle produced is reflected in the various demands for changes, both from middle classes and the labouring poor. They were together in demanding Parliamentary Reforms and fought against the landed interest to repeal the Corn Law. But thereafter their interests and movements diverged with working class movement finding independent expressions in Chartism and Ludditism and culminating in an organised political party in form of the Labour Party. That however was much later. In the 1840s real income per head, in the world's first modern nation, was falling. Such an alarming statistic made the possibility of social revolution quite real. That it did not happen was in large measure due to a second phase of industrialisation, based on coal, iron and railways, which soon followed the first phase.

Check Your Progress 4

- 1) Was it possible for the 'Poor Law' to promote capitalist development?

.....

.....

.....

.....

.....

- 2) Why did the interests of the working class and the capitalists converge to a certain extent during the initial phases of the industrial revolution? Why did it diverge later on?

.....

.....

.....

.....

.....

2.7 LET US SUM UP

In this unit we discussed the roles of the domestic market and the external market in England's industrial revolution. The domestic market was larger and more stable while growing at a slower rate. The external market, on the other hand, was more dynamic although having a fluctuating rate of growth. Population, per capita income, distribution, tastes, etc. determine the size and composition of the domestic market. Not only comparative advantage, but the strong mercantile tradition and military prowess determined, in case of mercantilist England, its composition and growth of international trade. England had colonies across the globe. Even the comparatively more developed colonies like India were converted from an exporter of manufactures to that of raw materials and importer of British manufactures by the early 19th century. 'Drain of Wealth' from colonies to the metropolis (England) was accentuated by the triangular pattern of trade. Mercantilist England's active state policies fostered her dominance in the sphere of international trade. The State pursued protectionist policies through imposition of steep tariff barriers and quotas against imports of final manufactured textiles from India and other countries. Since the mid-nineteenth century, British foreign trade policy tended to be guided more by the doctrine of laissez faire. But by then England had emerged as the only industrial and internationally most competitive country of the world. Hence she could do away with protectionist policies at least as long as other competing nations like Germany had not emerged.

In this unit, you have also read the prominent role cotton textiles played in Britain's industrialisation. Hence cotton textiles has often been described as the 'leading sector' in fostering the world's first industrial revolution. However, cotton, being a consumer good has fewer backward and forward linkages than iron, a capital (and a

producer's) good. The iron industry, it may be noted, contributed to Britain's industrialisation only since the mid-19th century when railways came in a big way.

In Britain's capitalist development, the poor were oppressed and exploited. The State sided with the capitalists and passed anti-poor laws, so as to generate a reserve army of 'free labour readily available for employment by capitalist at a low wage rate. It shows that Britain was not having a 'laissez faire' policy after all.

Note that with sole emphasis on maximising profits, the demand side was completely neglected. Domestic wages, kept at subsistence level, could not promote demand for industrial goods. Hence Britain faced industrial stagnation in the 1830s and 1840s and rising political discontent since the mid-nineteenth century.

2.8 KEY WORDS

Labour Power : Capacity to do work.

Leading Sector : A term coined by W.W. Rostow to denote the sector that plays a dominant role in country's industrial revolution. In case of Britain it was cotton industry, a light consumer goods industry. In case of USSR the heavy industry was the leading sector.

Primary Accumulation : Accumulation is the addition to the stock of capital. Primary accumulation is accumulation—in case of Britain, through coercive external trade and forced enclosures—prior to the development of industrial capitalism. It is a necessary condition for a country's industrialisation.

Revolution : A structural and a drastic change as contrasted with a systematic and continuous change.

2.9 SOME USEFUL BOOKS

Deane Phyllis, 1967. *First Industrial Revolution*, Cambridge University Press, London.
Hobsbawm, E.J. 1968. *Industry and Empire*, Penguin Books, London. Chapters 2, 3 and 4.

2.10 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) Read Section 2.2 and answer.
- 2) Read Sub-section 2.2.1 and answer.
- 3) Read Sub-section 2.2.2 and answer.

Check Your Progress 2

- 1) Read Sub-section 2.3.1 and answer.
- 2) Read Sub-section 2.3.2 and answer.
- 3) Read Sub-section 2.3.2 and answer.

Check Your Progress 3

- 1) Read Section 2.4 and answer.
- 2) Read Sub-section 2.4.1 and answer.
- 3) Read Sub-section 2.4.2 and 2.4.3 and answer.
- 4) Read Sub-sections 2.4.3 and 2.4.5 and answer.

Check Your Progress 4

- 1) Read Section 2.5 and answer.

UNIT 3 THE RISE OF COMPETING NATIONS, EXPORT OF CAPITAL AND THE FIRST WORLD WAR (1870-1914)

Structure

- 3.0 Objectives
- 3.1 Introduction
- 3.2 Rise of Monopoly Capital and Emergence of Competing Nations
- 3.3 Trends of Growth Preceding the Age of Imperialism
- 3.4 Character of Monopoly Capital
- 3.5 Dramatic Rise in Britain's Foreign Investment
- 3.6 Territorial Expansion of the Great Powers
- 3.7 Emerging Technical Backwardness of Britain
- 3.8 Let Us Sum Up
- 3.9 Key Words
- 3.10 Some Useful Books
- 3.11 Answers/Hints to Check Your Progress Exercises

3.0 OBJECTIVES

After going through this unit, you should be able to:

- discuss how competitive capitalism based on a large number of small firms in the industrial sector gave way to a gradual concentration of economic power in a few firms giving rise to what is known as monopoly capitalism;
- analyse the reasons behind the relative decline of Britain's industrial hegemony and the rise of competing nations;
- explain the sectoral change in Britain's industrial output in the second half of the nineteenth century and Britain's direct foreign investment; and
- describe the underlying factors behind colonial expansion of the advanced capitalist countries.

3.1 INTRODUCTION

By the middle of the nineteenth century, Britain had established itself as the leading industrial power of the World. Its emergence as the "workshop of the world" arose from the fact that starting with "textile industrialisation" (Unit 2), growth was soon diversified to producers goods, and growth was preserved through dominance over international trade, both with the underdeveloped colonies and the developing countries. This dominance in trade was, in turn, reinforced by the monopoly of Britain as an industrialised nation as well as through a colonial pattern of trade.

The importance of international trade for British industrialisation cannot be overstated. It was critical for industrial expansion because of

- Britain's poor agricultural raw material base
- inadequacy of domestic food production and
- relatively small size of the home market for industrial output of mass consumption, arising from a low ratio of wages in national income.

3.2 RISE OF MONOPOLY CAPITAL AND EMERGENCE OF COMPETING NATIONS

industrial power, posed by the newly industrialising countries — France, Germany and U.S.A. These countries required imports of machinery, technical expertise and of finance from Britain to build up their own industries. In order to protect their infant industries from the competition of initially lower-cost British manufactured goods, they erected tariff and other trade barriers to the import of these goods, such as, textiles. Once their own industrial base was strong, they could dismantle tariffs and emerged as competitors to Britain, both in their own markets and in the international arena, particularly Germany and the USA. Thus, Britain no longer enjoyed undisputed industrial dominance by the end of the 19th century.

This period was characterised by the concentration of production into very large units especially in the late industrialising countries like Germany. This concentration was reflected in both the employment of workers and the means of production. In Germany in 1882, 0.9% of the enterprises employed 39.4% of the work force and 75% of steam and electric power. In the USA in 1904, 0.9% of the industrial enterprises employed 25.6% of the workforce and produced 38% of the total industrial output. This kind of concentration would itself lead to the monopoly in production of the handful of the big enterprises.

Apart from the concentration of capital because of the increasing size of enterprises, combination or integration of the production process was also taking place. In other words, if earlier different branches of industry were located in different production units, they were now carried on under the same roof as an integrated process.

Cartels or syndicates, which are mainly marketing organisations of a number of large firms, also rose to dominance in this period. These organisations decided on fixation of prices to maintain monopoly profits, restricted output and shared out the market among firms. The concentration and combination of capital as well as the formation of cartels implied the end of competition amongst a large number of small producers and distributors. It signalled the beginning of the era of monopoly capital, where a small number of cartels and business houses held almost complete sway over production and distribution.

The challenge to Britain's industrial hegemony gave rise to a competition amongst the advanced countries in national and international markets. Monopoly capital further sharpened this rivalry because of the need to find new and ever expanding avenues for the profitable investment of capital as well as markets for industrial output. This rivalry between industrial nations eventually expressed itself as imperialism — accumulation on a world scale leading to a struggle for control over and economic conquest of the underdeveloped regions of the world.

3.3 TRENDS OF GROWTH PRECEDING THE AGE OF IMPERIALISM

The period between 1840 and 1870 saw a rapid increase in the pace of industrialisation in Britain. Growth shifted from the textile industry to the capital goods industry. So did exports, as you can see in Table 3.1.

Table 3.1: Principal Exports as a Proportion of total Domestic Exports 1830-70

	1830	1850	1870
Cotton yarn and goods	50.8	39.6	35.8
Other textiles	19.5	22.4	18.9
Iron, Steel, Machinery, Vehicles	10.7	13.1	16.8
Coal, Coke	0.5	1.8	2.8
Others	18.5	23.1	25.7
	100.0	100.0	100.0

Source: E.J. Hobsbawm (1968) *Industry and Empire*, p. 10.

The reason for the expansion of the capital goods industries were two fold. The first was the demand from rapidly industrialising advanced countries like USA and Germany.

profitable investment, which found an outlet in the application of the steam engine to goods and passenger traction on a large scale, namely, the railway boom.

The railway boom (1830-1850) was most important in this second phase of industrial expansion. The railway construction took place in two spurts, a small one in 1835-7, and a big one during 1845-7 within Britain. By 1850, £ 240 millions were invested in the railways alone. This expansion of railway construction, apart from being a new means to mobilise capital accumulation, had other very important consequences owing to the strong linkages both of the backward (stimulating the materials production required for railways) and forward (opening up new raw material sources and markets) kind.

The railways were responsible for the increased demand for, and thus domestic production of, iron, steel and coal, (Table 3.2) This, in turn, implied an industrial revolution in these heavy industries, and both a deepening and a widening of the base of industrialisation.

Table 3.2: U.K.'s Output of iron, steel and coal (in million tonnes)

	Pig-iron	Steel	Coal
1850	2.25	0.049	49.0
1880	7.75	1.440	147.0

Source: E.J. Hobsbawm (*ibid*) p. 116.

The railway boom went a long way in diffusing social upheaval through its direct and indirect impact on employment and wages. At the peak of construction, the direct employment was of at least 200,000 people. The number of coal miners increased from 200,000, in 1850, to half a million, in 1880. Thus, there was an increase in jobs available for the unskilled workers, who were drawn off the rural surplus labour force.

The employment of the skilled labour in engineering goods and machine building industries also doubled between 1850 and 1881. Though wages in general did not increase to any significant extent, there was respite to be gained from a greater availability of both skilled and unskilled jobs.

The stimulus given to production by the railway boom would have petered out quite soon, had the railway construction remained confined to Britain. But it did not: Europe and N. America saw a positive expansion of the railways in the three decades after 1850, followed to a lesser extent by other countries.

The growth of the railways abroad provided a continuing outlet for the export of capital from Britain for financing the foreign railway construction (on which the Governments borrowing from Britain usually guaranteed a return). Additionally, the export of steel rails, locomotives and rolling stock, made in Britain, was greatly stimulated.

Table 3.3: World Railway mileage opened per decade (to nearest thousand mile)

Year	United Kingdom (UK)	Europe (including UK)	America	Rest of the World
1840-50	6000	13000	7000	—
1850-60	4000	17000	24000	1000
1860-70	5000	31000	24000	7000
1870-80	2000	39000	51000	12000

Source: E.J. Hobsbawm, (*ibid*), p. 115.

The world railway mileage rose from around 20,000 in the decade 1840-50, to over 100,000 three decades later. This huge mileage of the railways was built largely with British finance, using British materials and British contractors and engineers. It is hardly surprising that a small nation of barely 30 m. in the mid-19th century continued to dominate the world. Its economy was continuing to expand rapidly and ever larger interest earnings started flowing in on the capital invested abroad.

The export of capital was thus given a strong impetus by the expansion of the railway construction abroad. By 1870, over £700 million was invested abroad, a fourth of which was in USA alone. This capital export also encouraged investment in industrial shares and, hence, resulted in the transformation of the capital market.

3.4 CHARACTER OF MONOPOLY CAPITAL

As we have seen, the distinguishing feature of capital in the late nineteenth century was the emergence of the monopoly capital. This was not restricted to industry and trade, but came to dominate banking as well. The emergence of the financial oligarchy can be illustrated from the experience of Germany.

Table 3.4: Percentage of Total Deposits in German Banks

	In 9 big Berlin Banks	In 48 banks with a capital of more than 10 million marks	In 115 banks with a capital of 1 to 10 million marks	In the small banks (with a capital of less than 1 million marks)
1907-08	47	32.5	16.3	4
1912-13	49	36	12	3

Source: V.I. Lenin (1952) *Imperialism, the Highest Stage of Capitalism*, p. 32.

Thus, nine banks controlled about half the deposits of the banking system. But this is only part of the story. The big banks had two other ways of mopping up banking finance. One was the opening up of branches all over the country. The second was to control the smaller banks through credit and ownership of shares of the small/medium joint companies. Thus, the big branches controlled a large number of affiliated banks.

Germany is but one example of the phenomena of concentration and monopoly in banking, which was echoed in the USA and Britain. Increasingly, the few large banks began to enter into monopolistic agreements with each other, and behaved like cartels and syndicates.

We have discussed above the concentration and centralisation of banking finance in the late nineteenth century. Though interesting in itself, this phenomenon assumes special significance when seen in the light of the transformation of banking finance to finance for industry, i.e., finance capital. The fusion between industrial and finance capital was the hallmark of monopoly capital. The coalescence between industrial capital and finance capital can be gauged from the following — the six big German banks were represented by their directors and board members in 751 industrial companies. Further, fifty one of the biggest German industrialists were on the board of these six big banks.

Therefore, three processes happened simultaneously and were inter related — the concentration in industry, the concentration in banking, and the fusion and domination of the industrial and financial oligarchy as Finance Capital.

Check Your Progress 1

1) What are the factors that led to a monopoly in production in a few enterprises?

.....

.....

.....

.....

.....

2) Why is a cartel antagonistic to the tenets of perfect competition?

.....

.....

3) Why was the railway boom so important in the second phase of industrialisation?

.....
.....
.....
.....
.....
.....

4) What is monopoly capital?

.....
.....
.....
.....

3.5 DRAMATIC RISE IN BRITAIN'S FOREIGN INVESTMENT

The other remarkable feature of the period after 1870 is the massive jump in investments abroad, or the export of capital. Export of commodities was always important for Britain, but the overseas investment increased at an unprecedented scale in the age of Monopoly Capital (Table 3.5).

Table 3.5: European Countries' Foreign Investment Stock, 1854-1913 (\$m)

Year	Britain	France	Germany	Others	Total (approx.)
1854	1100	—	—	—	1200
1862	1900	—	—	—	2000
1874	5000	1000	—	—	6500
1885	7000	3500	—	—	12000
1900	10000	5600	1450	4000	22000
1913	18300	8700	5600	11400	44000

Source: M.B. Brown (1978) *Economics of Imperialism*, p. 171.

The increase in capital exports was not restricted to UK alone. In fact, while in 1874 Britain accounted for almost 75% of the total capital exports of the world, by 1913 her share fell to 40% owing to the emergence of rival industrial nations as international investors.

Not only was there an increase in the capital accumulated abroad, but its direction in terms of geographical location also changed. It moved away from the advanced world to colonies, independent dominions and areas, where Britain exercised significant and effective control, like Latin America (especially Argentina).

Europe declined in absolute importance, its absorption of British capital falling by 50% between 1875 and 1913. After 1870, over 75% of foreign investment from Britain was in regions of recent settlement i.e. regions developed by the European immigrants, like Australia and South America. By 1913, 47% of the investment was in the British Dominions like India, Canada, etc., and this was the most crucial geographical shift.

Even in those periods when domestic investment was more than foreign investment, the quantum and share of foreign capital formation was very high between 1870-1913.

Table 3.6: Britain's domestic and foreign investment in relation to National Income

	National Income (£m)	Investment as Percentage of National Income		
		Foreign	Home	Total
1865-69	845	4.5	6.2	10.7
1870-74	1060	6.9	6.4	13.4
1875-79	1080	2.4	7.7	10.2
1880-84	1140	5.0	5.7	10.8
1885-89	1215	6.5	3.8	10.3
1890-94	1360	4.7	4.2	8.9
1895-99	1560	2.7	5.9	8.6
1900-1904	1720	2.2	8.2	10.4
1905-1909	1880	6.7	5.2	11.9
1910-1913	2120	9.3	4.1	13.4

Source: M.B. Brown (1974). *The Economics of Imperialism*, p. 176.

This massive investment of capital abroad was made possible, upto the 1820s, by a favourable balance of trade in commodities and in services such as insurance and shipping. After the 1870s, however, the very large increase in income from abroad, by way of interest and dividend on previously exported capital, financed further foreign investment.

The story of the financing of capital exports from Britain is, in fact, quite complex. In international trade and investment, the balance of payments must always balance. Country B (Britain) can invest in country A (America) usually only if country B has a surplus on current account vis a vis country A (because investing abroad would be a debit item on B's balance of payments and this must be financed through a corresponding extent of credit on the current account). Otherwise, there would be problems of balancing the balance of payments. In reality, however, Britain invested heavily in America, (N. America and Argentina in particular) despite not having a current account surplus with America or with Europe most of the time. Conversely, Britain invested very little in colonies like India and Malaya despite a large current account surplus with them. This is because Britain found it profitable to use the foreign exchange earned by countries like India and Malaya (through their export surplus to America or to Europe) to pay for her own trade deficit with N. America and Europe and thus be free to export capital to America. The colonies played a crucial balancing role, enabling Britain to carry on a smooth process of profitable capital exports to the fast-growing developing areas like America, without the process being disrupted by balance of payments problems. Similarly Britain invested heavily in Europe despite not having a current account surplus, with no problems, because of the large Indian export surplus to Europe the proceeds which were under British control. In 1913, it is estimated that India had a surplus of £45 million vis a vis Europe, whereas Britain was running a balance of payments deficit of £60 million with Europe. A very large share of this deficit was thus financed by India's export surplus earnings alone, over which Britain had absolute control. (See S.B. Saul, *Studies in British Overseas Trade* in this connection).

The question of why Britain chose to invest much more in the temperate developing areas rather than in her own tropical colonies is related to the fact that the former were

- politically independent,
- growing fast and were
- settled by emigrants from Britain with a permanent stake in the development of these areas.

All these factors raised profitability in these regions, compared to low levels of economic expansion in the colonies which had to remit a hefty share of their tax revenues to Britain through unilateral transfers in the form of export surplus.

Table 3.7 : Foreign Investment

	Current account balance of trade (Lm).	Incomes from Overseas Investment (Lm)
1870-79	50	53
1880-89	75	75
1890-99	99	97
1900-13	90	145
1911-13	206	188

Source : D. Aldcroft & H.W. Richardson, *The British Economy : 1870-1939*, p. 64.

To sum up the discussion upto now, there was a massive spurt after 1870 in the export of capital from Britain, both in absolute amount and as a proportion of total capital formation. This was increasingly financed by earnings on previously invested capital abroad and towards the end of the century was redirected geographically from the industrialised world to the temperate British dominions which were settled by Britons, such as Canada, Australia and S. Africa; and also to Argentina in Latin America.

The export of capital was directed towards areas of low risk and secured returns - loans to governments or mixed public and private ventures. In fact, 50% of foreign investment was so directed. Of this, 70% went into areas of social overhead capital i.e. public utilities and infrastructure. Finally, the return on this investment was usually guaranteed by the local government. Therefore, the high surpluses accumulated due to Britain's monopolistic position as the first industrialiser in the earlier period were directed to developing non-industrial countries.

The advantage from the export of capital were essentially four :

- i) a reduction in cost of imports due to improved infrastructure in the colonies and hence improvement in the relative price of British exports;
- ii) Access to valuable minerals, forest products and agricultural raw materials in the hinterland of the three continents (Asia, Africa and Latin America).
- iii) Access to new markets with infrastructure investment.
- iv) increasing invisible earnings by way of interest and dividends on capital accumulation overseas.

Table 3.8: Gross Domestic Capital Formation (GDCF) and Foreign Investment

	GDCF as per cent of GNP	Foreign Investment as per cent of GDCF	Total CF as per cent of GNP
1870-9	10.5	44.0	15.1
1880-9	9.2	62.1	14.9
1890-9	9.7	36.7	13.3
1900-9	10.6	41.6	15.0
1904-13	9.4	75.6	16.6

Source: Aldcroft and Richardson (1969) *ibid*, p. 120.

As has been shown in Table 3.8, there is a clear statistical evidence of a long run inverse relationship between foreign and domestic investment. Foreign investment was high in the early 1870s, 1880s, early 1890s and 1910s. Domestic investment was high in the middle and late 1870s and late 1890s, and 1900s. Further, foreign investment as a proportion of gross domestic capital formation was high and rising in the first set of periods.

Additionally, a large part of the domestic investment, especially fluctuation or net additions was in public services and utilities floated by local authorities.

Therefore, a pertinent question arises with reference to British economic development in this phase. Was domestic industry, especially new industry, growing slowly because it was starved of funds as a result of capital exports? Or alternatively, was the export of capital an outcome, of failing opportunities for domestic investment? If the latter was true, then foreign investment would be complementary to, rather than at the expense of, domestic investment. It would then play a stabilising role for British economic growth.

It is important to note that domestic and foreign investment need not be viewed entirely as alternatives. In other words, if capital exports had been halted, it does not follow that capital would have been invested alternatively within the economy. Surpluses may simply be consumed unproductively in the absence of profitable opportunities for investment. Domestic investment need not go into industry unless there is domestic demand for investment in the industrial sector.

That foreign investment was a "sink" for accumulated surpluses in the absence of profitable domestic opportunities can be argued more convincingly. As will be discussed later, the British economy had become extremely sluggish in this period, and was not innovating and adopting productivity raising and competitive technology in industry. Whenever this did happen, as in the bicycle boom in 1893-5, large amounts of capital was invested domestically. In fact, extremely risky investment in hotels and "single strip companies" were also undertaken at home. A study of the automobile industry also indicates that the paucity of funds was not the cause of its slow progress. Thus, the slow pace of development in new industry resulted in very few avenues of profitable domestic investment. When it did occur, it was in the local authorities sponsored utilities rather than industry. Given the existence of non-industrial colonies and dominions, capital flowed overseas. Colonies thus provided an opportunity for profitable investment of capital that lacked investible opportunities within Britain.

Check Your Progress 2

- 1) Name the countries which exported capital overseas. Also name the countries which were importers of capital.

.....
.....
.....
.....

- 2) Normally exporters of capital are those countries which run a surplus in their current account in the balance of payments. Then, while Britain had a current account deficit in the balance of payments with the American countries, how could it invest (i.e. export capital) in those countries?

.....
.....
.....
.....
.....
.....
.....

3) Why did Britain invest more in temperate countries like the USA than in tropical countries like India?

.....

.....

.....

.....

.....

4) Discuss the economic advantages accruing to the exporters of capital.

.....

.....

.....

.....

.....

5) Account for the 'push' and 'pull' factors that led to a dramatic rise in Britain's foreign investment in the late nineteenth century.

.....

.....

.....

.....

.....

3.6 TERRITORIAL EXPANSION OF THE GREAT POWERS

The period between 1876 and 1914 witnessed a rapid spurt in the acquisition of colonial territory by the advanced countries. At the end of this period, no significant areas of the world were left unconquered, and any further gains could be made only through repartition. In other words, the division of the world into regions of control was complete and only redivision was possible.

Table 3.9: Colonial Possessions of the Great Powers
(million square kilometers and million inhabitants)

Country	Colonies		Metropolitan		Total			
	Area 1876	Popln. 1876	Area 1914	Popln. 1914	Area 1914	Popln. 1914		
Great Britain	22.5	251.9	33.5	393.5	0.3	46.5	33.8	440.0
Russia	17.0	15.9	17.4	33.2	5.4	136.2	22.8	169.4
France	0.9	6.0	10.4	55.5	0.5	39.6	11.1	95.1
Germany	-	-	2.9	12.3	0.5	64.9	3.4	77.2
USA	-	-	0.3	9.7	9.4	97.0	9.7	106.7
Japan	-	-	0.3	19.2	0.4	53.0	0.7	72.2
Total for 6 Great Powers	40.4	273.8	65.0	523.4	16.5	437.2	81.7	960.6
Colonies of other Powers (Belgium, Holland, etc.)							9.9	45.3
Semi-colonial Countries (Persia, China, Turkey)							14.5	361.2
Other countries							28.0	289.9
Total for whole World							133.9	1657.0

Source: V.I. Lenin (*Ibid*), p. 95

From this table, a few notable trends emerge.

- a) The increase in colonies in terms of area was 50% after 1876 upto the eve of the first World War, for the six big powers. This area of colonial possessions was one and a half times the area of the six colonies.
- b) The young capitalist countries, i.e. USA, Germany and Japan began with no colonial possessions in 1876. By 1914, they had acquired about 15% of the newly colonised territories.
- c) Of the older powers, France had industrialised in this period and was under the dominance of monopoly capital. It had acquired about 40% of the increase in colonial possessions between 1876-1914. Russia's colonial territory was more or less unchanged in this period.
- d) The most obvious areas for redivision in the initial stages were the possessions of the small states like Belgium etc., as well as the territories with a semi-colonial status.

Upto now, the focus has been on control over colonial territory or political subjugation of a large part of the world to a few great powers. But there is yet another method of economic and commercial subjugation which gives rise to positions of intermediate dependence on the metropolitan countries. The semi-colony is one such example, and China was the typical example with all major European countries as well as Japan, carving out their spheres of economic concessions.

Another striking case is South America, especially Argentina. The investment by British finance capital was estimated to be of the order of 8.75 billion francs in 1909. A contemporary commentator chose to characterise Argentina as a 'British Commercial colony', despite its political independence. Portugal, in return for being a British Protectorate, had granted Britain several commercial and trade privileges in its former S. American empire, and Brazil was another important sphere of commercial influence for Britain.

However, even excluding such dependencies from the total, by the beginning of the first World War, 80% of the world's area was accounted for by colonial possessions and metropolitan countries. Thus, at the end of the rapid territorial expansion in the period of monopoly capital, the desire for further acquisition could only be realized through a redivision of the world.

3.7 EMERGING TECHNICAL BACKWARDNESS OF BRITAIN

In a world of competing industrial nations, and the threat to British hegemony over industrial production, some loss of ground for her industry was to be expected. But the story of the period between 1870-1914 is not only of the emergence of effective contenders to British industrial prowess, but also one of economic stagnation or even retardation within Britain.

Table 3.10: Average Annual Rates of Growth of Selected Economic Indices of the UK

	Net National Income	Real Income per head	Output per man hour	Industrial Production	Industrial Productivity
1860-70	3.0	2.5	—	2.9	1.1
1870-80	1.9	0.8	0.9	2.4	1.2
1880-90	4.2	3.5	3.8	1.6	0.5
1890-1900	2.1	1.2	1.3	2.8	0.2
1900-1913	1.1	0.4	0.6	1.6	0.2
1870-1913	2.3	1.3	1.5	2.1	0.6

Source: Aldcroft and Richardson (1969) *ibid.* Compiled from Tables on p. 4 and p. 126.

From the above table it is evident there was a slowing down of growth in this period, despite some years of transitory spurts. When compared with other countries, Britain's performance was one of the poorest amongst the big powers (Table 3.11).

Table 3.11: Average Annual Rates of Growth of Domestic Output and Output per man hour 1870/71-1913

	Output	Output per man hour
France	1.6	1.8
Germany	2.9	2.1
USA	4.3	2.4
Canada	3.8	2.1
Sweden	3.0	2.7
UK	2.2	1.5

Source: Aldcroft & Richardson (*ibid*) p. 7.

If manufacturing is taken separately, the relative position of Britain is even more dismal (Table 3.12).

Table 3.12: Average Annual Rate of Growth in Manufacturing (percentage)

	UK	USA	Germany	France	World
1900-13	1.7	5.3	4.7	2.5	3.0

Source: Aldcroft and Richardson (*ibid*) p. 105.

Thus, it can be safely concluded that both in terms of intertemporal rates of change within Britain, and in comparison to the total as well as manufacturing experiences of other industrialising countries, the performance of the British economy was very poor.

The growth in industrial and economic activity in this period can be traced to essentially four factors.

- a) While the early phase of industrialisation was based on simple inventions which were the outcome of practical skill and experience, after 1870 the importance of scientific knowledge, experimentation and technology became critical. The two high growth industries of this period, namely the electrical and chemical industries were based entirely on the development of Science and Technology. The Germans were world leaders in both these industries. The development of the internal combustion engine was yet another example of the application of science and technology to industry. In all three cases, the USA followed Germany very closely.
- b) The extension of the factory system to areas left untouched in the earlier round was yet another change. This was accompanied by the mechanisation of machine making. The latter was first done in armaments, and effected a revolution in metallurgy.

Along with the extension of the factory system and automation, the scientific management of labour on the work floor was pioneered by the USA, a labour scarce economy.

- c) Industrial mass production increasingly aimed itself at the potential market of the working people in advanced countries. This was particularly true for the USA with its large domestic market for mass consumption goods, partly owing to its size and partly owing to a relatively more egalitarian distribution of personal incomes in a new settler economy compared to the European economies. The share of wages in national income in the USA was around 60 per cent, while in most European countries it was closer to 50 per cent in the inter-war period, for example.
- d) As discussed earlier, the USA and Germany displayed a very high degree of concentration and centralisation of capital and the emergence of monopolies, cartels etc.

Britain continued to have a rapid expansion in those industries where there was no need for technology upgradation or reorganisation of the production process. A prime example of this was ship building. The initial impetus for this came not from technical or quality advantages (French and American ships had an edge over British), but from growing production and trade, and the demand from her colonies.

When it came to those industries where large scale production and scientific technology were important, Britain's performance was often poor. This was the case even in areas where Britain was the pioneer as regards invention; commercial application of the invention however often took place faster in Germany or the U.S.A.

In the chemical industry, although Britain invented synthetic dyes, by 1913 she accounted for only 11% of world output, whereas the corresponding shares of USA and Germany were 34% and 24% respectively. In fact, Germany supplied 90% of the synthetic dyes to Britain.

Electricity is another case in point. From being world leaders till the 1840s, by 1913 the British electrical industry produced a third of Germany's output. The finance and expertise for the electrification of England's first underground train system in 1905 was American. was American.

The iron and steel industry is a very telling example. All the technical advances that were made between 1850 and 1880 were British in origin. Yet except for the Bessemer converter (1856) which made the mass production of steel possible, British industry failed to adopt most of the other inventions. In fact, Britain's industrial rivals, Germany and the USA benefited more from British inventions than did British industry. By the early 1890s, British production and productivity were lower than in USA and Germany, and by 1910 the US production of basic steel was almost twice Britain's total steel production.

The international position of Britain altered significantly in this period. As world industrialisation proceeded at a rapid pace, it was expected that British exports would face competition. However, Britain found herself outcompeted in manufacturing, trade and other exports.

Table 3.13: United Kingdom's Share in world trade (percentage)

	World Exports	World Imports	World trade in manufacturing	World manufacturing
1885	16.7	21.0	37.1	31.8
1913	13.9	15.8	25.4	19.5

Source: Aldcroft and Richardson (*ibid*), p. 65.

There was thus a decline in Britain's share of foreign trade. But there were also significant changes in the pattern of trade. Though the share of textiles declined, it was still high at 36.5% in 1913. Moreover, the decline of Britain's share in world exports was faster for the new industries than in textiles and coal.

Table 3.14: United Kingdom's Share in world production of selected industries (percentage)

	Machinery	Chemicals	Vehicles	Textiles
1900	39.7	28.0	48.0	47.6
1913	29.2	22.9	37.0	44.5

Source: Aldcroft and Richardson (*ibid*) p. 72.

Further, Britain was not able to even retain its superiority in old established products except perhaps for cotton textiles. Given its inability to compete effectively in the new industrial products, as well as preserve existing advantages, Britain had to turn increasingly to captive colonial markets to absorb its products.

Check Your Progress 3

1) Study Table 3.10 carefully. What conclusions can you draw?

.....

.....

.....

.....

- 2) What are the different types of subjugation carried out by the Great Powers? Briefly explain each of them citing examples.

.....

.....

.....

.....

.....

.....

- 3) Briefly highlight the nature of growth of industrial activity in Britain in the late nineteenth and early twentieth century and account for its relative decline as compared to the newly industrialising countries of this period

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

3.8 LET US SUM UP

In this unit, you have read that Britain's second phase of industrialisation was based largely on the expansion of her capital goods industries. The railway boom — with its backward and forward linkages — facilitated the expansion of capital goods industries like pig iron, steel and coal. When Britain's domestic investment slackened, her surplus capital found a ready outlet through direct foreign investment initially, in the then newly industrialising countries like Germany and USA and later in her colonies located in the temperate latitudes with a mere trickle flowing into the tropical colonies. Indeed, imperialist Britain's exploitation of the tropical colonies leading to their drain of wealth was the prime source of capital which Britain invested overseas.

There was a marked change in the industrial capitalism in Britain, in the second half of the nineteenth century coinciding with her second phase of industrialisation. The first phase was marked by a large number of small firms providing a semblance of capitalism characterised by perfect competition. In the second phase however, this gave way to monopoly capitalism with the rise of cartels and syndicates, a few large firms taking control over production and distribution of industrial output and a fusion between finance (banking) capital and industrial capital. This phase also marked the zenith of imperialism when the Great Powers brought under their hegemony by political, economic and commercial subjugation almost the entire globe (which is now known as the third world).

UK, as you have read in Block 1, was the first country to undergo the industrial Revolution. However, soon other countries like France, Germany and USA, rapidly industrialised and not only threatened Britain's industrial hegemony but also tended to outcompete her. UK gradually lost ground to USA, Germany, and France in the late nineteenth and early twentieth century in terms of productivity (output per man hour), rate of growth of manufacturing output, automation, industrial management and in areas where scientific knowledge was crucial for technological upgradation e.g. electrical and chemical industries. UK failed to maintain its position in the late nineteenth and early twentieth century in terms of productivity (output per man hour), rate of growth of manufacturing output, automation, industrial management and in areas where scientific knowledge was crucial for technological upgradation e.g. electrical and chemical industries.

where she was the pioneer in invention — e.g. iron and steel industry. No wonder that Britain's share in international trade and in industrial production declined although these continued to grow in absolute terms. Unable to compete with the then newly industrialising (and today's advanced) countries, Britain increasingly turned to the protected colonies to market her products.

3.9 KEY WORDS

Cartel: A marketing organisation of large firms that decide on fixation of prices to maintain monopoly profits, restrict output and share the market among them.

Monopoly capitalism: Capitalism characterised by a small number of cartels and business houses holding almost complete sway over production and distribution. Fusion between industrial and finance capital is the hall mark of monopoly capital. In Britain, monopoly capital dominated trade, industry and banking sectors, since the late nineteenth century.

Imperialism: A policy of acquiring dependent territories or colonising through trade, diplomacy and military conquest. Countries like Britain, France, Belgium, Germany and Italy were imperialists in the late nineteenth and early twentieth centuries.

3.10 SOME USEFUL BOOKS

Aldcroft, Derek H. and Harry W. Richardson, 1969. *The British Economy 1870-1939*. Macmillan and Co. Ltd., London.

Brown, Michael Barratt, 1974. *The Economics of Imperialism*, Penguin Books, London.

Hobsbawm, E., 1968, *Industry and Empire*, Penguin Books, London, Chapters 6, 7 and 8.

Hobson, J. A., 1988. *Imperialism: A Study*, Unwin Hyman, London.

Huberman, Leo 1981 *Man's worldly goods: The Story of the Wealth of Nations*, People's Publishing House, New Delhi.

Lenin, V.I. 1975. *Imperialism, the Highest Stage of Capitalism*, Foreign Languages Press, Peking.

3.11 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) Read Section 3.2 and answer
- 2) Read Section 3.2 and answer
- 3) Read Sections 3.2 and 3.4 and answer

Check Your Progress 2

Read Section 3.5 and answer all the questions.

Check Your Progress 3

- 1) Read Section 3.6 and answer
- 2) Read Section 3.6 and answer
- 3) Read Section 3.7 and answer

UNIT 4 INTERWAR YEARS (1919-39)

Structure

- 4.0 Objectives
- 4.1 Introduction
- 4.2 Effects of the First World War (1919-25)
 - 4.2.1 The British Economy
 - 4.2.2 The International Setting
 - 4.2.3 The Gold Standard
- 4.3 British Slump Amongst Booms and the Making of the Great Depression (1925-29)
 - 4.3.1 The British Experience
 - 4.3.2 The Gold Standard and the Policies of Major Countries
- 4.4 The Great Depression and the World Economy
 - 4.4.1 Causes of the Great Depression
 - 4.4.2 Effects of the Great Depression
- 4.5 The Great Depression: the British Experience
 - 4.5.1 Events leading to the Departure from the Gold Standard
 - 4.5.2 Effects of the 'Reversal'
 - 4.5.3 Gold Loses its Glitter
 - 4.5.4 Imperial Preference
- 4.6 Lost Chances and Britain's Relative Stagnation (1932-39)
- 4.7 Britain on the Eve of the Second World War
 - 4.7.1 Industry
 - 4.7.2 Employment
 - 4.7.3 Foreign Trade
 - 4.7.4 Government
- 4.8 Let Us Sum Up
- 4.9 Some Useful Books
- 4.10 Answers/Hints to Check Your Progress Exercises

4.0 OBJECTIVES

After going through this unit, you should be able to:

- discuss the effects of the First World War on the British economy;
- describe why the British economy slumped in the early 1920s when the world economy as a whole was enjoying the post-war boom;
- analyse the factors that led to the Great Depression of the 1930s; and
- find out why Britain lost out as the leading industrial and trading nation of the world in the inter war years.

4.1 INTRODUCTION

Fluctuations notwithstanding, the British economy had grown quite steadily till the First World War. It had already ceased to be the only or even the primary industrial power. Problems were already evident in the economy, in terms of falling growth rate of exports, inability to catch up with other industrial economies in the field of technological change, etc. But the situation looked, at least to most contemporaries, quite satisfactory. What Britain was losing in commodity exports was being made up by exports of services. While she was suffering from technological lag her network of trade and finance prospered. London reigned as the financial capital of the world and the wealth which it brought went a long way in making Britain, in the words of a contemporary observer "the best country to be rich and leisured in". Britain was primarily living off her colonies, her international capital exports and her position as the trading and financial centre of the world. But she was still living quite well. The First World War and the interwar years changed this, as the traditional economy of Britain not only ceased to grow but contracted. Britain emerged from the war as a much weaker economy and never quite recovered from it. The mantle of international leadership descended on the USA.

The evaporation of the old ways of doing business did not produce an equal change in the old ways of thinking. Much of what happened in Britain, and in other industrial countries, during this period can be put down with hindsight, to staggering intellectual myopia on part of the policy makers. The Great Depression which gripped the world in the late 1920s and early 1930s was in large part a creation of this outmoded orthodoxy. On the British case this was best exemplified by Churchill's decision to return to the gold standard in 1925. As we shall see below it was a very costly mistake. Keynes, the most incisive and often the only opponent of the ruling ideas, publicly wondered why Churchill did "such a silly thing". He was not heard; perhaps he made the mistake of being right, when men of greater reputation were wrong.

In any case policy makers in other countries also went on to do equally "silly things". Politicians and economists (most but not all of the latter group) gave poor accounts of themselves in this period, at least till middle 1930s. The recovery programmes launched then rescued many countries from the abyss of the Depression. For most part though the actions of those empowered to influence national economies were a striking example of Liebling's law: 'If men of adequately complex minds act with enough perversity they will succeed in picking themselves out of the door into the street.' Britain went out to the 'streets' in this period and never quite managed to get back to the comfortable surroundings of the Victorian classical economy. The initial impetus was, however, through the 'shock' of the first War. We discuss the effects of the War in the next section.

4.2 AFTER EFFECTS OF THE FIRST WORLD WAR (1919-25)

In this section we shall see how the immediate post-war boom which Britain enjoyed ended in a slump in the mid-twenties and how Britain gradually lost her status as the leading industrial nation of the world. We shall also see why the Gold Standard with its fixed exchange rate system did not prove to be a viable mechanism to save Britain from the impending Great Depression.

4.2.1 The British Economy

The difficulties of the British economy, as we had noted in Unit 3 Sec 3.7, had started in the 1870s. Industrial production from 1870s to 1913 increased at only 2% annually. This was already behind the growth rates of countries like the USA and Germany. This relative decline can be principally attributed to the relative fall in exports of goods, which were the 'engine of growth' in the early period of industrialisation. Exports grew less fast because other countries had meanwhile industrialised. No longer the 'workshop of the world', Britain could not hold on to its share of world exports. This loss in leadership had, however, less impact than one would have expected. The cushion provided by the large exports of invisibles (shipping, insurance and other commercial services) enabled imports to rise. The need for developing production for the home market was correspondingly reduced. Such a state of affairs could only have been temporary, since other countries could have developed their own services. The war accelerated the problems of the British economy. However the immediate effect of the First World War was a shortlived boom.

The Boom

The accumulation of pent-up purchasing power during the war and the reduction in the level of stocks created the conditions for a boom. As men were demobilised and factories were deluged with orders there was a sharp rise in economic activity. Production, employment and prices rose. The government maintained high levels of expenditure. By 1921, however, the boom had worked itself out. As imports from other countries started arriving, and domestic production caught up with pent up demand, credit restrictions were imposed, and the boom turned into a slump.

The Slump

When Britain was caught in an economic downturn, her principal competitors were still enjoying a boom. Construction activity seemed to be the dominant factor in producing booms in the USA, France and Japan. Curiously, Britain was suffering from a housing

shortage, and yet there was no 'housing boom'. Rent restrictions, high building costs and ineffective implementing authority (the much criticised, then as now, 'local authorities') were the reasons for the absence of the construction boom. However equally important reasons behind the British slump were its changed international position and the stringent credit conditions.

4.2.2 The International Setting

The war decisively altered the contours of the international economy. International power equations, in economic and political terms, were changed. The USA emerged as the strongest economy, while Britain and Germany were much weaker. Agriculture transformed from prosperity to poverty. The pre-war network of trade were altered: obstacles to trade both in terms of tariffs and currency fluctuations were recognised. In successive international conferences, including those in Brussels (1920) and Genoa (1922), recommendations were made for the removal of these obstacles, but to little avail. One major aspect of the pre-war international economy, in terms of its hold on the mind of the policy makers, came out unscathed: the Gold Standard. Although it was suspended during the War the idea was alive and kicking. The Genoa conference of 1922 reaffirmed the faith in the Gold Standard. The Cunliffe Committee appointed in Britain to consider its post-war monetary problems assumed that the gold standard would continue. Commitment to the Gold Standard was strong in the USA too, embodied in the form of Benjamin Strong, Governor of the Federal Reserve Bank. America emerged as the strongest economy after the war and made the adherence to the Gold Standard a condition for continuing to finance European reconstruction. Thus the pre-war manager of the Gold Standard, Britain and the post-war leader amongst the industrial nations, America were both steadfast in their belief in the 'old fashioned religion' — as Thomas Lamont had described the Gold Standard. The adherence to this system in the changed conditions on the post war era created the conditions for the Great Depression of the late 1920s. We discuss this in the next sub-section. Before that it will be useful to explain what the system of Gold Standard meant for the international economy.

4.2.3 The Gold Standard

The Gold Standard can be characterised by (1) free flow of gold between individuals and countries (2) the maintenance of fixed values of national currencies in terms of gold and hence each other (3) the absence of an international coordinating organisation. These three features meant that countries facing BOP deficits would experience outflow of gold to countries enjoying BOP surplus.

To maintain the fixed value of the currency, which comes under pressure when gold flows out, the economies would have to undertake deflation (forcing domestic prices to fall) so that the domestic price level can change suitably to maintain the exchange rate. The policy option of devaluation (downward revision of the value of one's own currency vis-a-vis foreign currencies) was ruled out in the Gold Standard. In the period between 1925-29, domestic and international policies of major countries were aimed to maintain the Gold Standard. The ineffectiveness of these attempts is a testimony to the altered conditions of the world economy and not to a lack of sincerity on the part of the policy makers.

4.3 BRITISH SLUMP AMONGST BOOMS AND THE MAKING OF THE GREAT DEPRESSION (1925-29)

1925 was a turning point in more than one way. The wranglings and recrimination about the treatment of Germany subsided with the Dawes Reparation Plan (1924) and the Locarno Pact (1925). This restoration of political stability (a fragile one, as it was proved later) was followed by the decision to return to the Gold Standard. For the world as a whole, the period between 1925 to 1929 was, by certain indices, good. Production of raw materials and food stuff increased by 11%, trade by 19% and trade in manufactures by 29%. America led the boom and lent to many other nations (2,192 million dollars, net) which enjoyed similar upturns. Two major nations were left out of the 'golden twenties' — Britain and Germany.

Table 4.1: Indices for Manufacturing Production (1913-100)

	World	Britain	Germany
1925	121	86	95
1929	153	100	117

Source : Lewis, A. (1949) : *Economic Survey*.

Note the considerably lower increase in the British and German indices by 1929 compared to the pre-war base, though over the four years, 1925-29, the percentage increase, is similar to that of the world average.

4.3.1 The British Experience

In Britain a grim reminder of the depressed conditions was the rate of unemployment, which was much higher than in other industrialised countries.

Table 4.2: Industrial Unemployment as per cent of Work-force Rates: 1925-29

Country	Unemployment Rate, Percent
USA	7.9
France	3.8
Germany	9.2
U.K.	12.0

Source: Eichengreen B. and Hatton T.J. (1988), 'Interwar Unemployment in International Perspective.

Almost all observers now agree that the British downturn was due to the decision to go back to gold at the pre-war parity; the consequence was an over valued pound. This harmed the British economy in two ways: (i) by making imports relatively cheaper thus restricting the development of new industries and (ii) by making exports dearer. The share of the British exports in international trade had been falling since before the war; but after 1925 it fell even in absolute volume. Added to this were specific reasons for the decline of particular export sectors: coal production was hurt because of mines being opened elsewhere and the development of water power, cotton owing to the development of Indian domestic production and Japanese competition in the Far East. Besides, iron and steel, ship building and metals were suffering from war time over-expansion. The combined effect of all these was a fall in exports and rise in unemployment. Most of the unemployment was concentrated in the export industries.

Table 4.3: Exports and Export Prices, average of 1927-29 (1913-100)

Country	Export Prices	Export Volume
France	101	147
Italy	123	136
Switzerland	149	101
UK	162	85

Source: Lewis *ibid*.

It was not that the authorities were not concerned with the overvaluation of the pound. They were, but the Gold Standard meant that they could only deflate and not devalue (as we have seen in Sub-Section 4.2.3). So prices were sought to be reduced by reducing money wages. The adherence to the Gold Standard meant that wages (and through them prices) had to be lowered. But in practice this led to a major social upheaval in the form of the 'general strike' from 4th to 13th May, 1926. The strike was sparked off by attempts to enforce wage cuts in the most depressed industry: coal. Mine owners proposed a cut which was rejected by the unions. The mines were 'locked out' by the owners who called on other workers to come out in solidarity. For a period of 13 days the response was enthusiastic but after the Trade Union Council decided to call off the strike, the protest fizzled out with only the miners holding out. However the effect on

wages (apart from the miner's wages) was not notable. The price index however did fall, from 160 in 1925 to 134 in 1929 (1913=100). This fall can be principally attributed to the restrictive credit policy adopted by the government. Interest rates were kept high by the Bank of England to attract short term capital and stabilize the pound. This had a depressing effect on domestic economic activity. Another contributory factor was the fall in agricultural prices, which was a result of substantial increases in production, relative to consumption (the former increasing due to technological breakthroughs and restoration of pre war average levels in Europe).

The later half of 1920s was thus a troubled time for Britain. The symptoms were known but the remedy was grossly wrong. No efforts were made to stimulate production for home consumption. It was an article of faith that come what may the Gold Standard was to be maintained — thus to this end, the domestic economy was compressed. The overvalued pound meanwhile merrily messed up British exports. All this was a very high price to pay for the 'pride of the British Pound sterling'. The sufferings caused by this myopia seemed grotesquely ironical in 1931, when, faced with increasing strain on the pound, Britain abandoned the Gold Standard. This double take did much to lessen the pains of Depression, but it implicated the political and economic leadership of Britain even more for causing the avoidable distress and privation of the 1920s.

We will now discuss the international operation of the Gold Standard to understand how the conditions for the Depression were created.

4.3.2 The Gold Standard and the Policies of Major Countries

As the British economy plunged into a crisis following 'the return to gold' other countries continued to try and prop up the system. In 1927, the US Federal Reserve undertook to lower interest rates so as to encourage capital flow out of the US and into Britain. This was to stabilise the struggling pound. However, the French Franc, which was undervalued (the French had declined to take on the full pains of deflation required by a return to pre war levels of exchange rates) attracted most of the gold. America and France accumulated gold, but they did not have to expand under the Gold Standard. But Britain had to depress its economy because of the Gold Standard. Therein lies the asymmetry in the working of the Gold Standard as a system. Between them the USA and France held 60% of monetary gold by the end of the 1920s. This was clearly in excess of their requirement, for they did not account for either 3/5 of world production or 2/3 of world trade. Another way of putting the same proposition, i.e. the US and France had excess gold reserves, is to say that they were not expanding their economies sufficiently. Monetary expansion should have been greater and fiscal expansion was not even seriously contemplated. If France and the US had expanded the resultant higher incomes would have increased imports, probably more than proportionately. This would have raised the import share and gold would have flowed out decreasing the supply of reserves. Both the franc and the dollar were undervalued and revaluation (the opposite of devaluation) could have been undertaken. The Gold Standard however prevented such a move. Revaluation was not in the policy options. The burden of adjustment fell entirely on the debtor countries. In the context of the early 1930s the burden was too strong and it destroyed the gold standard. From 1928 the Federal Reserve followed a contractionary policy to combat the speculation in the New York stock exchange. The Germans were also trying to eliminate speculation. All in all the Atlantic economy was in the grip of contractionary policies. The basic reason was the revival of the Gold Standard and the attempts which were made to sustain it in conditions no longer suitable for it. Policy making everywhere was such as to depress economic activity.

Check Your Progress 1

1) What do you understand by the 'Gold Standard'?

.....

2) What were the factors responsible for Britain's relative decline in the world economy after the first world war?

.....

One of the contentions of this orthodoxy was that larger public expenditure would destroy confidence and 'crowd out' private activity. The Keynesian solution of greater public expenditure to combat the fall in aggregate demand, so pervasively lauded and used later, was dismissed as "lingering illusions on part of certain commentators". Keynes' spirited opposition during the Macmillan Committee hearings fell on absolutely deaf ears.

Increasingly the people began to expect the deflation to continue. Their expectation was that prices would be even lower in future. This generally produces two effects: (a) people hold back purchases to take advantage of the expected lower prices and (b) they are reluctant to borrow at any money rate of interest because they would have to pay back effectively more when the prices are lower and the money rate of interest falls below the real rate (i.e. money rate deflated by the price level).

This certainly happened during the Depression, although lack of sensitive expectations - indicators means that we cannot date the beginning of this phenomenon. But by the spring of 1931 expectations had caught up with events, and people began to expect more deflation and postpone expenditure until deflation ended. Deflation also increased the real burden of debt thereby further curtailing expenditure.

Government response all through these times continued to be deflationary, barring the British *volte-face*. It were these interactions of national policies and individual reactions which produced the depression. Specific events contributed to the general trend. The First World War had changed the world economy. The votaries of the gold standard ignored this and in trying to force their outdated system on the world generated the Great Depression. Like the physicians who treated Mozart with mercury to cure his ailments, they not only failed to cure the disease, they also killed the patient.

4.4.2 Effects of the Great Depression

Statistics are a useful but often inadequate guide to historical events, even events in economic history. However, the downturn in Great Depression was so catastrophic that figures speak eloquently in this era. Here we present some of the important measures of the great slump:

Table 4.4: Production and Trade, 1929-37

	1929	1937
Food Stuffs		
World Trade	100	89
World Production	100	100
Raw Materials		
World Trade	100	81.5
World Production	100	74
Manufactures		
World Trade	100	59.5
World Production	100	70

Source: Lewis, *Op. cit.*

With the slump came a decline in foreign investment and fall in primary product prices. Most of the debtor countries were primary producers and this decreased their ability to import manufactures. However the reason why trade contracted more than production is because of erection of various trade barriers. Following the lead given by the American Hawley Smoot Tariff of 1930, tariffs all over increased sharply.

Table 4.5: Impact of the Depression in various countries:
Index of Industrial Production (1929 = 100)

Country	Industrial Production Index in 1932
USSR	183
USA	53
Germany	53
France	72
UK	84

USSR was of course insulated from the world economy. Japan attacked the slump with expansionary policies which were followed only mutedly, if at all, in Britain and completely cold shouldered in the US and Germany.

Table 4.6: Unemployment in Industries (1930-38)

Country	Unemployment Rate
US	26.1
France	16.2
Germany	21.8
U.K.	15.4

Source: Eichengreen and Halton, *Op. cit.*

Unemployment was the biggest social consequence of the Depression. The sharp rise in unemployment in US, France and Germany, relative to the 1924-29 period (compare Table 4.6 with Table 4.2) compared to the milder change in the British unemployment rate is a testimony to (a) British economy's decline in the pre-1929 period as compared to upswing in other economies (b) the fall of the other economies into an abyss in the post 1929 period as compared to a milder slump in Britain.

Table 4.7: Wholesale Price Indices in 1932 (1929 = 100)

Country	Index
USA	67.5
Germany	70
France	65
UK	75

Deflation, of course, was pervasive and substantial. The British figure is higher due to the effects of abandoning the Gold Standard in September 1931, but still appreciably less than 100.

Other figures and events can be cited. But the above figures do convey the depth of the slump. Our main concern is with Britain and now we turn to the depression in its British manifestation.

Check Your Progress 2

1) Was deflation an antidote for the ills of early 1930s? Explain.

.....
.....
.....
.....
.....
.....
.....

2) What was the effect of the Great Depression on the macro economic indices of the developed countries?

.....
.....
.....
.....
.....
.....

4.5 THE GREAT DEPRESSION: THE BRITISH EXPERIENCE

As already stated the Depression in Britain was milder. The principal reason was because of the decision, forced and taken with great distaste, to leave the Gold Standard in September 1931. Such was the hold of the orthodoxy that apart from that little else was done to encourage activity. Britain escaped the worst but lost the chance to do much better.

4.5.1 Events Leading to the Departure from the Gold Standard

The slump from 1929 onwards affected trade and this in turn reduced the 'cushion' in British BOP, the invisibles. From 1929 to 1931 earnings from invisibles reduced by 180 million pounds. This produced a negative balance of trade (exports suffered by volume, the index falling from 104 to 69 [1927 = 100] but with primary prices falling the net barter terms of trade moved in Britain's favour, and thus exports by value fell by lesser amount). The adverse balance combined with a general loss of confidence in the British economy led foreigners to recall their assets. Together this resulted in an abnormal loss of gold for Bank of England. Pressure on the Pound increased in mid-1931. The Bank refused to increase the interest rate to punitive levels (fearing correctly, that the consequences would be appalling in an already depressed economy). Instead French and American credits were spent in defence of the pound. The Labour Government of the day somewhat dampened the fiscal contraction by refusing to cut unemployment benefits. Measures for sustaining the value of the pound would have been nothing short of being draconian. British policy was unprepared to go to the extent of the 'iron chancellor of Germany, Brüning, whose deflation was nothing short of being ruthless. Thus hemmed in, there was no choice but to abandon the Gold Standard.

4.5.2 Effects of the 'Reversal'

The devaluation following this agile policy shift was beneficial to the British economy. It lowered British export prices, relative to foreign prices and allowed the option of a more permissive monetary policy (which was taken up after a half year delay).

Imports becoming dearer, were cut. Devaluation checked the fall of prices in Britain (while they continued to fall in countries still on gold). Lower export prices (relative to foreign prices) helped maintain exports. The share of Britain in world exports increased between 1931 and 1933.

Table 4.7: Exports, Imports and Balance of Trade: 1931 and 1933

	Imports (1927=100)	Exports (1927=100)	Balance of Trade (Million)
1931	103	69	-104
1933	90.5	70	-51

Source: Mitchell B.K. (1980) *European Historical Statistics, 1750-1975*.

The effect of British devaluation on a world caught in throes of the depression was not particularly beneficial. If gold had flowed out of Britain allowing other countries to undertake monetary expansion the impact of the relative price change of those countries could have been mitigated. As it happened the Bank of England took this opportunity to build up its gold reserves — thus the effect on the rest of the world was deflationary.

4.5.3 Gold Loses its Glitter

Nothing not even the inflexible minds of the 1920s and 1930s policymakers could ignore the pressures created by depression. In 1933 the US came out of the gold standard and in 1936 the French followed suit. Other countries were not far behind. Most policy makers did not like it, but they had little choice by then. They had created and nurtured the depression, how the depression gobbled up their article of faith -- the Gold Standard.

The effect of this all round abandonment on Britain was to offset the gains she had made between 1931-33, when she was the sole devaluing country. British share of world exports, which had gone up to 10.37% in 1933 declined to 9.8% in 1937. However, the British colonial system, a great source of economic dynamism during the early years of British industrialisation came to the partial rescue of the mother country. The system devised was named, appropriately and without a trace of irony, Imperial Preference.

4.5.4 Imperial Preference

In 1932 countries of the Commonwealth met at Ottawa, Canada. They agreed to extend to each other increased import preferences to British goods.

Agreements were also 'worked out' with smaller countries, dependent on the British market so that they would increase their imports from Britain. Coal was the principal beneficiary of these later agreements.

The effect of these agreements on British trade was striking, as the following figures show:

Table 4.8: Share of UK in Imports of Various Countries in 1929 and 1937

Country	1929 (%)	1937 (%)
Australia	40.0	42.6
Canada	15.0	18.2
South Africa	43.1	46.3
New Zealand	48.7	50.2
Argentina	17.6	20.7
Sweden	17.3	19.0
Norway	21.2	24.6
Denmark	14.7	37.7

The first four countries in Table 4.8 belonged to the Empire and the latter group of four were the 'agreement countries'. Thus Britain increased its share of trade in these countries. One loss from this elaborate system of protection was that Britain did relatively poorly in unprotected markets. Foreign competition was deflected in these markets further worsening the British performance, which had already started lagging. The loss in unprotected markets was enough to outweigh the gain from protected ones and British share of world trade declined.

Check Your Progress 3

1) Why did value of British exports fall less than the volume of exports during the depression? What is its implication on Britain's capacity to import?

.....

2) Why did Britain have to abandon the Gold Standard?

.....

3) What was the effect of devaluation on the British economy during 1931-33?

.....

- 4) What was the effect of competitive devaluation of currencies of other advanced countries on the British economy during 1933-37? How did the British colonies contribute to her rescue?
-
-
-
-
-
-

4.6 LOST CHANCES AND BRITAIN'S RELATIVE STAGNATION (1932-39)

Britain, we have seen, did not suffer as grievously as the other industrial countries did. Paradoxically she also did not recover as well as some of the others, especially the US and Germany. This was principally due to the vacillation by the government on the issue of expansionary policies. There was some support for the special areas (the euphemism for areas particularly hard hit by the depression) and unemployment dole was increased. But political support for further changes in fiscal and monetary policy was not forthcoming. The Bank of England raised the rate of interest, partly to replenish reserves and partly to fight inflation. Prices however were nowhere near alarming levels. The trust of the government's policy was, as Hawtrey put it, to cry "Fire, Fire in Noah's flood".

Some increase in economic activity was possible as world output and trade recovered, led by the expansionary regimes in Germany and the US. This external stimulus was joined by a housing boom of respectable dimensions. Partly this was because of a difference in interest rates between consols and mortgages, which meant that funds flowed into building society. Another reason which was also responsible for creating the rate differential, was that the Bank of England finally exercised the option of pursuing an easy monetary policy which helped lower interest rates. Construction and its allied industries accounted for 30% of the change in income between 1932 and 1937. Fiscal policy, however, continued to be influenced by the tenets of orthodox public finance.

Two other, rather ineffective, public interventions were made in this period to boost the stagnating industries. For some industries, the particularly hard hit ones coal, cotton, iron and steel and shipbuilding efforts were made to maintain rates of profit by supporting monopolistic arrangements. In case of shipbuilding and iron and steel some new investment was made, but generally the arrangements prevented the emergence of new and efficient firms since the policy was to protect markets by quotas for everybody, irrespective of their efficiency. In fact, such a policy also made the declining industries more inefficient than they otherwise would have been and restricted investment in them.

The second policy was of tariff protection, for both industry and agriculture. But the levels were too low to stop employment from declining in the protected sectors.

Table 4.9: Annual Averages for Prices, Interest rates, Production and Employment; Britain 1921-29 and 1930-37 (1913=100, except for column 5)

Year (1)	Prices (2)	Interest Rate (3)	Production (4)	Employment (%) (5)
1921-29	154	4.57	86	88.2
1930-37	102	3.52	99	83.2

Source: Lewis, *Op. cit.*

Figures clearly show the failure of the British economy to achieve a strong recovery.

4.7 BRITAIN ON THE EVE OF THE SECOND WORLD WAR

The two decades between the two great wars were instrumental in significantly altering the structure of the economy which had grown up during the 18th and 19th centuries. We will now take a look at these changes.

4.7.1 Industry

Industries like cotton, iron, coal and shipbuilding were hard hit and lost their primary positions in the economy. Most of these were export oriented, and as we have seen, exports in this period was adversely affected by a number of factors. The bleak international scene forced many industries to turn inwards. The lesson that home market can be an important source of growth was learnt, although not fully implemented, in this period. Still, on balance, industries concentrating on the home markets did better in this period than the export oriented ones. Industries like automobiles, metal products and various consumer goods expanded. Many of the new industries were also technologically complex and geared towards mass production. This also helped in the turn to the home market. Some of the move in technologically advanced industries like aircraft and electrical products also relied on government backing for their growth. The 'voodoo economics' of 19th century, which said that wages of workers must be minimum to promote expansion, was unlearned in this era. Travails in export markets made the home market important and with it higher wages were recognised as a source of mass demand. Thus the industrial pattern changed, in terms of sectoral importance, technology and market orientation.

Another important change in industry was increasing concentration. Till 1914 Britain was one of the least concentrated economies, with the small family firm still dominating, barring some cases like public utilities and heavy industries. However the war, the slump and government encouragement helped to increase economic concentration markedly in this period. Before 1914 there were few monopoly products but by 1935 at least 170 products were mainly produced by industries comprising less than four firms. Compared to 130 railway companies in 1914, there were 4 in 1921. Most of these concentration were outcome of the idea of maintaining profit by eliminating competition. The result was restrictive and protective but not efficient. As in export sectors, in the domestic front too British industry was no longer competitive.

British industry also failed to regain the technological leadership which she had started to lose since the 1880s. In part this was due to the failure to undertake systematic research and development, especially the latter, namely turning discoveries or inventions to commercial practicability. A second source of this relative archaism was the availability of imports which often made obsolete technology profitable. Iron and steel industry did not adopt the Gilchrist-Thomas 'basic' process till late 1930s because they could import non-phosphatic ores cheaply and easily. Other factors — mostly sociological in origin — may have also contributed. The result was that in 1939 British industry was neither competitive nor technologically dynamic compared to the other advanced countries.

4.7.2 Employment

As the pioneering in industries of Industrial Revolution cotton, coal and shipbuilding lost ground. Employment in these industries declined. We have already noted the high figures of unemployment of this period. What gave unemployment in these years special character was their concentration in selected areas, primarily those areas which were dependent on the industries which faced a crisis. Eight out of ten workers in Jarrow, a small town in North England, were out of work from 1933 onwards as this town was entirely dependent on a shipyard which closed down. Examples like this were strewn across the country where unemployment seemed permanent and the places became derelict. The government, wedded to the principles of 'sound' public finance, did not provide much succour. It renamed the affected areas a 'special areas' -- this mealy-mouthed euphemism being symptomatic of its virtual inaction. Even when expansion could have been promoted it was not, and the misguided efforts to help particular industries did not promote much employment (or for that matter much industrial growth). It was not until 1941 that unemployment rates came down substantially.

4.7.3 Foreign Trade

Interwar Years (1919-39)

Britain's overseas transactions changed substantially in this period. The share of exports in production fell continuously. Imports ceased to grow more rapidly than industrial production. The balance on current account was negative from 1934 onwards.

Table 4.10: Trade Relative to Production.

Year	Exports/Production percent	Index of Imports as ratio of Industrial Production (1913 = 100)
1924	24	121
1937	15	114

Source: Mitchell *Op. cit.*

The process of adjusting the British economy to a smaller volume of trade had begun, but only partially. Imports, relative to exports were larger and financed through Britain's earnings on the capital account. The opportunity to restrict imports and promote domestic production more vigorously was lost in this period. In 1946 when invisible earnings declined substantially and terms of trade became unfavourable the problems of restricting imports came to the forefront. International trade lost its pre-eminent position in this period, although the decline had begun earlier. Appropriately one of the shibboleths of the Victorian era, "Free trade" also met with its formal demise in this period, when in 1931 Britain left the gold standard. The special conditions which had nurtured it had gone and with them its utility.

4.7.4 Government

The first war had seen the government taking over several industries. It also engaged in output control, licensing and price fixing. Import duties were imposed on some commodities (British automobiles being a lasting beneficiary of this, since the duties on them were retained even after the war). Although the post war decontrol was hasty and the ideology of *laissez faire* still powerful (exemplified by the return to gold standard in 1925), these public interventions showed that state involvement was both feasible and useful. One would resent state intervention but could no longer claim that they do not work. The slump produced more government actions in the sphere of industry. Most of these were in terms of promoting cartels and price fixing arrangements. It also started regulating prices and outputs by legal compulsion, especially in agriculture. Of course the other pillar of *laissez faire* namely free trade collapsed too, as noted earlier.

The sphere where orthodoxy held out was public spending and to a lesser extent monetary policy. Depression did not lead to a welfare state but rather its opposite. Salaries and benefits were cut producing a Naval Mutiny (1931) and hunger marches. In part such a difference in treatment of business and labour was a reflection of the political power balance of those years. Political pressures from the labour party declined after the 1920s (especially after the 'National Government' of 1931). It was also due to the convenient piece of reasoning by the representatives of business and their spokespersons; while increasing welfare expenditure was akin to "creeping socialism" (to borrow the words of a post Second World War British Prime Minister). Government help to industry was so vital for the national economy that the consequent observation of orthodoxy had to be tolerated.

Orthodoxy won the day, in the sphere of expansionary policy too, as noted earlier. Government's role in this period thus showed both signs of fundamental change and the hold of earlier ideas. It was Britain's misfortune that this continuity and change combination was unsuitable for the task of combating most of the economic ills of this period.

Check Your Progress 4

- 1) What were the factors responsible for Britain's not recovering as fast as other advanced industrialised countries? What were the roles of fiscal, monetary and commercial policies in this regard?
-

France and USA belonged to the former category while Britain belonged to the latter category. However, this did not materialise. Instead countries enjoying surplus also maintained old expenditure levels or even raised interest rates to curb speculation when reflationary policies were the need of the hour. This plunged the capitalist economies into the Great Depression. Industrial production, employment, volume and value of foreign trade and the price level, all fell drastically. Banks 'failed' and the stock markets crashed. While Britain was in the throes of recession for a much longer period, the impact of Depression in Britain measured by the indices mentioned above, was milder because Britain was the first country to devalue her currency in 1931 when she came out of the Gold Standard.

However, the beneficial effects of devaluation were only temporary as other competing countries also devalued their currencies later on to increase their share of world exports. Britain, then increasingly pursued protectionist policies by imposing tariffs and quotas. It also sought refuge in the protected markets of her colonies through a system known as Imperial Preference. Moreover, Britain increasingly relied on the home market for growth and expansion. However, the operation of the foreign trade multiplier with respect to Germany and USA offset to a certain extent the difficulties Britain faced in terms of price competitiveness:

4.9 SOME USEFUL BOOKS

Eichengreen B. and T.J. Hatton, 1988. *Inter War Unemployment in International Perspectives*.

Hobsbawm, E.J., 1969. *Industry and Empire* Penguin Books, Chapters 9, 10, 11 and 12.

Mitchell, B.K. (1980). *European Historical Statistics, 1750-1975*.

4.10 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) Read Appendix to EEC-01 Block 8. Unit 18 and Sub-section 4.2.3 and answer.
- 2) Read Sub-section 4.2.1 and answer
- 3) Read Sub-section 4.3.1 and answer
- 4) Read Sub-section 4.3.2 and answer

Check Your Progress 2

- 1) Read Sub-section 4.4.1 and answer
- 2) Read Sub-section 4.4.2 and answer

Check Your Progress 3

- 1) Read Sub-section 4.5.1 and answer
- 2) Read Sub-section 4.5.1 and answer
- 3) Read Sub-section 4.5.2 and answer
- 4) Read Sub-section 4.5.3 and 4.5.4 and answer

Check Your Progress 4

- 1) Read Section 4.6 and sub-section 4.7.4 and answer
- 2) Read sub-section 4.7.1 and answer
- 3) Read sub-section 4.7.1 and answer
- 4) Read sub-section 4.7.3 and answer

UNIT 5 JAPAN ON THE EVE OF THE MEIJI RESTORATION

Structure

- 5.0 Objectives
- 5.1 Introduction
- 5.2 Feudalism in Japan : 1600-1868 (the Tokugawa Era)
 - 5.2.1 Economic and Political Structure
 - 5.2.2 The Agrarian Basis—Rent and Tax
 - 5.2.3 Structure of the Japanese Village
- 5.3 Evolution and Change under the Tokugawa Peace
 - 5.3.1 Specialisation and the Growth of Exchange
 - 5.3.2 Sankin-Kotai and the Merchant Class
 - 5.3.3 Rise in Productivity—Sources and Effects
- 5.4 The Question of the Burden on the Peasantry and Indices of Peasant Discontent
- 5.5 The Impact of the West on Japan
- 5.6 Let Us Sum Up
- 5.7 Key Words
- 5.8 Some Useful Books
- 5.9 Answers/Hints to Check Your Progress Exercises

5.0 OBJECTIVES

After reading this unit you will have an idea of:

- the structure of Japanese economy and society before the age of modern economic growth starting in 1868
- the changes within this structure which led to capitalist production and social tensions conducive to change
- the catalytic effect of the impact of Western penetration.

5.1 INTRODUCTION

The study of Japanese industrialisation has been of great interest to students of economic history and of development problems alike, owing to two factors. First, Japan has been the only Asian country to achieve an independent route to capitalist industrialisation starting in the third quarter of the 19th century. Second, an unprecedented speed of transformation of economic and social structure has marked this process such that within a few decades Japan was challenging the established European and N. American powers not only at the economic but also at the political level; while its post second world war reconstruction and growth has been so rapid that it now ranks as the second largest economy in the world after the U.S.A.

Scholars of Japanese development from the west tended to adhere at first to a somewhat simplistic view that it was the coercive impact of the western powers on Japan which shook it out of its feudal lethargy and initiated the process of modern development. Recent research substantiates the more

realistic proposition, however, that very significant trends of growth of exchange relations, of productivity, and of capitalist enterprise marked the late Tokugawa era and provided the conditions which were conducive to change. The specific timing of the political transition known as the Meiji Restoration may have been determined by the Western impact, but it is necessary to go back to a study of the developments in the Tokugawa period in order to appreciate the long-term basis of the transformation.

5.2 FEUDALISM IN JAPAN 1600-1868 (THE TOKUGAWA ERA)

The origins of Japanese feudalism go back to the 8th century A.D. We take up the story however, only in 1600, when the Battle of Sekigahara was fought, in which Tokugawa Iyeyasu led a confederation of clans to victory against an opposition coalition of clans and established the **Tokugawa Shogunate** (or Regency) in 1603 which was to rule Japan for the next two and a half centuries. The clans which had fought alongside Tokugawa were known as the **fudai** while those which had comprised the opposition were the **tozama** or 'outside' hans.

5.2.1 Economic and Political Structure

The economic basis of Japanese feudalism as indeed of feudalism anywhere, was the appropriation of the agricultural surplus from the peasantry without payment, by a class of overlords. The details of the system of estimation and collection of the agricultural surplus are discussed in the next section. Here let us consider the overall structure of Japanese society in this period.

About four-fifths of the entire population consisted of the peasantry, who cultivated the land, which they held in units of varying size, on the condition of payment of fifty per cent of rice output to the overlord, known as **daimyo**. The whole of the area of Japan was divided into a few hundred **hans** or territorial units, each under the control of a hereditarily ruling clan led by a noble, the **daimyo**. At the beginning of the Tokugawa era the daimyo numbered 194, while at its end the number of hans and of daimyo had increased to 266. The daimyo maintained large bands of armed warriors, or **samurai** apart from their personal retainers. All were maintained out of the surplus produced by the peasantry, the **samurai** being given stipends in rice by the **daimyo**.

About 75 to 80 per cent of the total cultivated area was under the various hans of the daimyo while the remaining 20 to 25 per cent was under the direct control of the shogunate, a part being assigned for the maintenance of the Emperor's establishment. Although the titular head and sovereign in Japanese society, the Emperor was in practice powerless and led a shadowy existence surrounded by the **kuge** or nobles of ancient lineage, in Kyoto. The Tokugawa ruled in the Emperor's name from the capital city, Edo (known as Tokyo in modern times), through the **Bakufu** (loosely translated as 'military dictatorship'). The Shogunate maintained its own troops, known as **hatamoto** out of the rent-cum-tax collected from its territories.

The **samurai** class was quite numerous, making up 6 to 7 per cent of the population: while if the other members of the ruling class and their personal retainers are added, some 9 to 10 per cent of the population can be said at that time to be engaged in no productive work contributing to material output. The remaining 10 per cent of the non-peasant population was made up of artisans and merchants, ranging from the small-scale pedlars to the

Feudal society in Japan was characterised by a very rigid hierarchy. Only the ruling classes—the nobility headed by Shogun and Emperor, and the warrior class of Samurai—had any social status and political rights within the system. Merchants, artisans, peasants and those providing services were without any political rights and were assigned a very low social status. The formal division under the Tokugawa was into four classes by rank (known as the **shi-no-ko-sho** structure), considering the population other than the Emperor, Shogun and daimyo: **shi** referred to the samurai, **no** to the peasants, **ko** to the artisans and manufacturers, and **sho** to the merchants. Beneath these four groups however there were further divisions of people considered so 'sub-human' such that they were not fitted into the formal categories: these were termed the '**hinin**' or literally, non-people, and below them in turn were the **burakumin** or outcastes who were the ethnic Japanese. None other than the daimyo and samurai were permitted to carry arms.

The daimyo with his warriors resided in a fortified castle, around which clustered the habitations of the civilian population providing goods and services for the consumption of the nobles and their establishment. The castle-town, or **joka-machi** was also a centre for the activities of the merchants trading in agricultural and manufactured goods. Few villages in Japan were more than 20 miles away from a **joka-machi**.

As Japan is a system of four islands, ports dealing in trade had developed such as Osaka, Nagasaki, Yokohama and Kagoshima. In the early Tokugawa period Japanese traded extensively with the Asian mainland countries and piracy along the coast of China by Japanese ships was common. Alarmed by the incursions of the European missionaries and traders, the Shogunate forbade by 1638 any external trade and also banned travel abroad by the Japanese. In consequence Japan became virtually a closed economy, with only a handful of Dutch missionaries and private traders being permitted by the local daimyo to remain on a small island, Deshima in Nagasaki bay. Shipping therefore became restricted to coastal trade within Japan.

Manufacturing production was on an artisanal basis. Cotton and silk textiles and articles of everyday use were produced. The artisans were organised into guilds, as were the merchants. The town of Nishijin was an important centre of silk textile production. Osaka was the main centre for the activities of the merchants or **chonin**. It was estimated that nearly three-quarters of the mercantile wealth of Japan was concentrated in Osaka. A fairly high level of urbanisation had been reached by the 18th century in Japan. By 1730, Edo was probably the world's largest city with over half a million inhabitants while both Osaka and Kyoto reached this size by 1800. With several large ports and castle-towns, it is not surprising that urban population was about 22 per cent by 1800.

5.2.2 The Agrarian Basis—Rent and Tax

The main crops grown in Japan were rice—accounting for over 75 per cent of cultivated area—millets, cotton, hemp, oilseeds, and mulberry on which silk worms were raised. At the beginning of the Tokugawa period each village was more or less self-sufficient in producing nearly every other crop besides the basic foodgrain, rice.

The agricultural surplus was extracted from the peasantry in the form of a rent-cum-tax paid in rice. It was a **rent** to the extent that the decentralised feudal domains, the **han**, were under the hereditary proprietorship of the **daimyo** who collected this surplus. It could be called a **tax** to the extent that upto a quarter of the territory was controlled by the central government of the Shogunate which similarly collected the surplus in kind. Unlike in

European feudalism, labour-services contributed by peasants for cultivating land directly under the **daimyo** or **Shogunate**, was never prevalent. (However some labour services were performed by poorer peasants for better-off holders of land within the village, as will be discussed below in sub-section 5.4.3).

Although the **daimyo** obtained their feudal revenue in the form of rice, they naturally needed to convert a part of it into cash for purchasing their requirements of manufactured goods. Quite a substantial part of their rice revenue was distributed in kind as stipends to their **samurai**, from whose ranks the **han** administrative staff were also drawn. The remainder was partly retained for consumption and the bulk was sold to merchants. Under the Tokugawa, periodic surveys were carried out at intervals of several decades, to estimate the area under rice and its yield per **cho** (one **cho** equalled 2.45 acres). Half of the estimated rice output was taken as the rent-yielding capacity. Each **han** therefore had an estimated revenue measured in physical volume units of rice (the **Koku**, equal to 4.96 bushels). The size and importance of a **han** was measured by this index. While the average **han** enjoyed about 10,000 **Koku** of revenue, Satsuma, one of the largest **hans**, had 70,000 **Koku** in rice revenue.

The rise in productivity in agriculture which occurred during the later part of the era meant that as a proportion of the actual rice output, revenue to the **daimyo** was declining below the fifty per cent estimated on the basis of earlier, lower levels of production. This entailed certain economic consequences which are discussed in sub-section 5.3.3.

5.2.3 The Structure of the Japanese Village

We have referred to the village population as 'the peasantry', but in reality the holders of land in the Japanese village were highly differentiated. There were those who held substantial area, known as the **jinushi**, forming a minority of leading families; while the majority comprised medium to small and very small holders of land known as the **kosaku**. By 'holders of land' we should not understand modern forms of landownership with rights of mortgage and transfer. Such concepts arise only with capitalist production. The landholders in the Japanese village had a hereditary right of occupation and cultivation of the land subject to payment of the rent-cum-tax to the overlords who represented the feudal proprietary class.

The **jinushi** were generally sufficiently well-off not to cultivate the land with their own manual labour, but employed the labour of farm servants in various forms of tied or bonded status (the **fudai** and **genin**), or gave their land and sometimes also livestock and implements, to poorer peasants from the **kosaku** lacking both, in return for labour services provided by these customary tenants or **nago**. The output was then shared in a proportion highly favourable to the **jinushi**.

Among the **kosaku** there were those medium scale holders of land who possessed enough implements and land to cultivate on an independent basis. Large numbers of the **kosaku** however had too little land to be able to obtain a subsistence. They were obliged to take some land as tenants (**nago**) from the better off cultivator in return for the performance of labour services in cultivating the land retained by the **jinushi** and sometimes they also used the latter's equipment. The poorest households provided the **genin** or farm servants working for life for the richer households, and in times of harvest failure the very poorest were obliged even to sell their children as slaves to the latter. This was probably the origin of the **fudai** who had the status virtually of slaves in the hereditary service of the richer households. Although the system was a paternalistic one based on personal relationships,

5.3 EVOLUTION UNDER THE TOKUGAWA PEACE

The period 1600-1858 was marked by relative peace. Hence the term 'Tokugawa Peace'. This period witnessed increased specialisation and productions for the market which gradually eroded the self-sufficient han economy. Also, the old feudal set-up, while retaining its rigid, hierarchical social structure, was changing to give rise to new powerful economic categories from the socially backward strata. Let us now look at all these issues in a greater detail.

5.3.1 Specialisation and the Growth of Exchange

The self-sufficiency of the hans gave way to increasing specialisation in production in the course of the 18th century. The long period of peace was conducive to this. Areas particularly suited to growing particular crops like cotton, or hilly areas suited for mulberry, devoted a higher proportion of area to these specialised crops while other areas with a larger proportion of valley land, increased paddy production. The corollary of specialisation in agricultural production was rise in the extent of commoditisation of products (a higher share of a given crop being sold) and a rise in inter-regional trade.

The source of information for changes in the cropping pattern, input use and yields for the 18th century are the detailed farm budget records kept by the literate section of the village population, namely the leading landholders controlling the bulk of the area. These records provide valuable insights into the nature of technical changes taking place in agriculture as well.

It appears that the position of all those who employed the labour of others in production, not only in agriculture but also in other sectors, must have improved substantially owing to the inflationary trend in the Tokugawa period. Rice prices rose more than 11 times between 1620 and 1850, mainly owing to the successive debasements of the currency which were undertaken by the Shogunate to meet recurrent financial crises. These crises arose owing to the fact that revenues from customs were non-existent and from excise very low, so the predominant source remained agricultural production, which could show periodic downturn thus reducing state revenue which was a share of the output.

Under the conditions of secular inflation and increasing market-orientation, the traditional agrarian relations tended to be modified over time towards more impersonal, even contractual relations. The status of the hereditary **fudai** and **genin** changed from the customary basis increasingly towards bondage on account of debt: the **nago's** status approximated towards that of the contractual tenant. The landowners and employers found it less paying to continue with kind payments to workers or with giving share of the output in kind to these tenants and slowly tried to substitute cash payments. Given stagnant output price inflation thus meant a downward pressure on the real earnings of labour and a profit inflation for all employers.

The well-to-do in the village started investing in the processing of agricultural products on a wider scale. These activities included hulling paddy, ginning cotton, pressing oilseeds, and the numerous stages of silk textile production from raising the worms on mulberry leaves to winding the thread in filatures and weaving the cloth.

Brewing of 'sake', an alcoholic drink made from rice, was another important activity. A rural dispersion of textile manufacturing and other activities thus marked the later half of the Tokugawa era. Artisans continued to engage in textile production in the major cities, particularly to meet the requirements of

the aristocracy for fine silks and brocades. But the increasing demand arising from the prosperity of the **chonin** (merchants) and the rural minority of well-to-do, was met through the development of an extensive 'domestic' or 'putting-out system' under which the merchants financed production by village cultivators-cum-artisans to whom they gave out the raw materials for spinning and weaving, or to whom they advanced cash for purchasing raw materials.

5.3.2 Sankin-Kotai and the Merchant Class

In order to maintain control over the great **daimyo** particularly of the **tozama** **han**, the Shogunate had instituted a system of 'alternate attendance' known as **sankin-kotai**. The **daimyo** had to spend some time attending the Shogun's court at Edo in alternate years, and when they returned to their castle-towns they had to leave their families as hostages at Edo. This system was designed to discourage revolt by the **daimyo**, each of whom had a territorial base and armed contingents at his command and could potentially pose a political challenge.

Owing to the **sankin-kotai**, each **daimyo** had to maintain two establishments, one of the **joka-machi** and the other at Edo, and incur the costs of regular travel to and from Edo, (which could be substantial for the more distant **han**). This system had several consequences. Roads and communications were developed and well maintained from the more than 250 **han** to Edo. A trading and associated financial system developed under which the merchants purchased a large part of the rice-rent of the **daimyo** for cash, and arranged to store it in warehouses and transport rice supplies as required to urban areas. Sometime the **daimyo** required cash for meeting his expenses at Edo even before the rice-rent had been obtained; the **chonin** concerned would then give a promissory note on the security of the future rice rent, against which cash could be obtained by the **daimyo** from the merchants' offices at Edo at a discounted rate. Thus bills of exchange and cheques came to be widely used in the late Tokugawa period. The richer merchants engaged in banking activities, accepting deposits and advancing loans. Not only the **daimyo** but the Shogunate itself was dependent on the leading merchant houses for financial accommodation in times of difficulty. Despite the growing economic importance and wealth of the merchants, especially of that section engaged in urban trade and banking, within the feudal system their social position remained very low. There was no legal protection for the **chonin** against forced loans (**goyokin**) exacted by the aristocracy, or against seizure of their assets. This contributed to the growing dissatisfaction of the **chonin** with the system. Even though they did not try to assert themselves, this discontent found expression, when the opportunity arose from the 1850s, in supporting the movement for political change which culminated in the Meiji Restoration of 1868.

The **samurai**, as part of the warrior-base of aristocratic rule, enjoyed a high social status even though the economic position of a large section of them was declining. This occurred because owing to the long Tokugawa peace there was no occasion for the **samurai** to use the martial skills in which they continued to be trained. They represented increasingly a functionless class, and the **daimyo** felt the **samurai** to be a drain on their rice-rents. Many **daimyo** started reducing the rice stipends of the **samurai** under them so as to have more income available for themselves to maintain ever higher standards of conspicuous consumption. While the **chonin** were becoming wealthier but had no political rights and low social status, the **samurai** on the contrary were increasingly impoverished though with a continuing high social status within the rigid structure of feudal society. Not all **samurai** were equally badly off: those engaged in administrative tasks on the **han** maintained their

economic status. But numerous samurai became ronin leaving their original han and wandering as masterless peripatetic warriors. Large numbers congregated at Nagasaki and Kagoshima.

5.3.3 Rise in Productivity—Sources and Effects

The farm budgets maintained by well-to-do households in the village indicate that along with specialisation and the growth of exchange, the nature of agricultural production was also changing from the mid-18th century. Firstly, the farm budgets show that expenditure on wages paid to hired labour went up compared to total expenditures, indicating that the customary employer-labourer relation of hereditary fudai and genin providing only subsistence, were giving way to payments made to hired workers.

Secondly, a rising trend is observed in the proportion of outlays on purchased manures and fertilisers. These do not refer to chemical fertilisers which were unknown at that date, but to fishmeal and urban sewage which was treated and purchased on a commercial basis by farmers for spreading on their fields.

The increase in use of inputs which had to be purchased required a corresponding increase in the fraction of output which had to be sold in order to finance these purchases. With the more intensive application of commercial manures and possibly also of labour, yields of the major crops definitely showed an upward trend.

There is also evidence of increasing attention being paid to measures of water-conservation in order to increase the area under irrigation which permitted a more widespread cultivation of rice. Improved varieties of rice were being evolved slowly through selective breeding. Technical changes which raised labour productivity included more efficient seed-drills and a simple instrument for threshing.

To sum up, a series of changes were taking place—a larger area under irrigation, more output of irrigated crops, higher yields from land owing to this factor and to more intensive use of commercial manures and labour, and higher labour productivity. The net effect was to raise land productivity considerably; the rate of rent-cum-tax however continued to be estimated on the basis of earlier, lower levels of rice production.

Because of the growing divergence over time between the rent-cum-tax as a fraction of earlier estimated output (one-half) and the rent-cum-tax as a fraction of actual output (about one-third by the end of the Tokugawa era), the village landlords benefited greatly. They could keep the benefits of rising production for themselves and in fact this must have been a major motivation for their undertaking more intensive cultivation in the first place. As an example, suppose that a well-to-do big landowner produced one thousand koku of net rice output earlier on which 500 koku had to be handed over to the daimyo. As a result of more irrigation, shifts in cropping pattern and more intensive cultivation with manures, production rises to 1,500 Koku, but this is not recorded officially. The landowner continues to pay 500 koku to the daimyo, keeping now 1,000 koku for himself compared to 500 koku earlier.

The prosperity of the well-to-do minority of big landholders showed itself in their investing their surplus increasingly in the agro-based processing sake-brewing and textile manufacture to which reference has been made in 5.2.2. The landowner of this type increasingly also became a landed entrepreneur or oyakota.

Check Your Progress 2

- 1) What was the impact of inflation on the traditional agrarian relations during the Tokugawa era?
.....
.....
.....
.....
.....
.....

- 2) What is the 'putting-out system'?
.....
.....
.....

- 3) What were the consequences of Sankin-Kotai on the Japanese economy?
.....
.....
.....
.....
.....

- 4) What were the sources of a rise in productivity in the Japanese economy? Who reaped its benefits?
.....
.....
.....
.....
.....
.....
.....
.....
.....

5.4 THE QUESTION OF THE BURDEN ON THE PEASANTRY AND INDICES OF PEASANT DISCONTENT

Even though the land rent-cum-tax as a proportion of the (rising) rice output was declining, the benefits of this does not seem to have gone to the majority of the peasants who operated medium and small holdings. Rather it was the better-off minority in rural areas who enriched themselves and went in for rural entrepreneurship as we have seen.

Indeed the majority of the peasantry appeared to be more discontented and under greater economic pressure, as the effects of price inflation and monetisation of the economy affected them adversely. There were two main indices of peasant discontent and resistance during the late Tokugawa period. First were passive forms of resistance like **infanticide**, the incidence of which

increased so much that the Shogunate felt obliged to promulgate a law banning it. It is very likely that many more female babies were killed by their poverty-stricken parents than were male babies, given the gender bias towards males which is prevalent in all Asian societies. Mere legal bans however could have little effect where economic necessity drove people to these acts.

The second form of resistance was **peasant revolts**. These were quite frequent and took the form of attacks on money-lenders and on landlords, the burning of documentary evidence relating to indebtedness and attacks aimed at corrupt officials. There were 71 separate cases of peasant jacqueries in different provinces during the period 1844 to 1859 alone. Over the entire period of Tokugawa rule more than 600 peasant uprisings took place.

The larger section of the peasantry thus formed a discontented and politically mobilisable force, and it supported the moves for a change in the old feudal order which were to be initiated in the 1860s by leading samurai and progressive daimyo of the **tozama han**.

The position of the poorer section of the peasantry was worsened by the tendency towards greater concentration of land ownership which is clear from the records. The price inflation contributed to this, for those poorer cultivators who did not produce enough rice for their needs and had to purchase it on the market using wages earned through labour, found it difficult to make ends meet. They borrowed and on failure to repay the use of the land in their possession, passed to their creditors. They themselves became tenants of their creditors who were often the leading landholders of the village.

5.5 THE IMPACT OF THE WEST ON JAPAN

Economic historians from the Western countries generally—with very few exceptions—interpret the impact of the West on Eastern societies as being liberating for the latter, in breaking down outmoded feudal institutions and initiating modern growth. A radically different interpretation is provided in the following perspective from the pen of Mao Zedong, a leading Asian revolutionary of this century.

“What is the ‘impact of the West’? It is the effort of the Western bourgeoisies.... to remould the world after its own image by means of terror” (1949).

In fact, the effects of the ‘impact of the West’ have varied depending on whether the Asian country experiencing the impact, came under Western colonial domination, or not. The unique feature of the relationship of Japan and the Western powers was that the latter attempted to dominate Japan, but did not succeed because the internal social structure in Japan underwent an upheaval leading to the establishment of a nationalist regime committed to rapid development and modernisation.

The Western powers’ drive during the first half of the 19th century to acquire colonial territories in Asia was aimed mainly at India and China, both populous countries with rich natural resources and ancient civilisations.

Japan was a far less attractive prize from the Western point of view. The Japanese feudal aristocracy had the advantage of learning from the unhappy experience of the other Asian countries, and they could see the tide of Western domination approaching closer while themselves being subject to

The highly educated section of the Japanese nobility mainly belonging to the *tozama han* and the *ronin* among the samurai, learnt of Asian developments at the same time that they read books on 'western science'. They saw most of India by the 1820s passing under the control of the British East India Company, which seized Rangoon in 1819 and embarked on the annexation of Burma. An illegal trade in opium grown in India was carried on by the British with China despite the Chinese Imperial ban on such trade. When the ban was sought to be implemented seriously, Britain launched the Opium Wars from 1842 to 1844 to bombard with warships the Chinese ports like Canton, and forcibly opened them to trade. Since Japan was so near the Chinese mainland, the opium wars and British victory particularly worried the Japanese aristocracy, to whom it was clear that Japan's turn could not be far off once China was colonised. The Unequal Treaties which the Chinese feudal regime was forced to sign, resulted in the ceding of Shang Jian (mispronounced Hong Kong ever since) to the British, the granting of 'extraterritoriality' (foreigners in the Treaty ports were not subject to Chinese law), and began the process of the major western powers vying to carve up China into their spheres of influence. Apart from the European powers, the USA too had launched an expansion across the Pacific, seeking to obtain refuelling facilities in countries like Japan with the main objective being the vast Chinese market.

The first attempt to penetrate Japan commercially was the voyage of Commodore Perry of the USA in 1853 and the signing of a treaty with the Bakufu the next year which did not mention trade, but effectively allowed American ships the use of two Japanese ports. The U.S. interest in Japan was renewed four years later when Townsend Harris extracted a trade treaty in 1858 from the Bakufu on very harsh terms for Japan. The other Powers scrambled to do likewise and a series of Unequal Treaties followed in quick succession in 1858 itself, with Holland (Aug. 18) Russia (Aug. 19) Britain (Aug 26) and France (Oct. 9). The Bakufu simply could not resist the pressure of the colonising powers who had acquired a territorial foothold in China.

The unequal treaties obliged Japan to turn herself into an open economy, through a clause which forbade her to raise tariffs above 3 per cent. In the Treaty ports the foreigners were not subject to Japanese law, ('extraterritoriality rights'), as in the case of the Chinese treaty ports. The Treaties were extremely unpopular within Japan and the fact that the Bakufu was obliged to sign them, exposed its bankruptcy to the Japanese people.

Japan was fortunate however that a sustained effort by the Western powers either singly or in combination, to colonise her, did not take place during the crucial decade 1858-1868. For during this time the Bakufu was tottering, internal movements for change had not emerged in a coherent form, and any hypothetical Western military assault on Japan at this time would certainly have led to her political subjugation. A very important period of grace was provided by the international conjuncture. The great rebellion in India, 1857-59 (which Britain called 'the Mutiny' and the Indians later called their First War of Independence) kept the British occupied, as did the consolidation of their position in China. Before that the Crimean War of 1854 had absorbed a great deal of British military energies. France was busy colonising Vietnam and was also tied down in Mexico. The USA could not follow up its initial lead vis-a-vis Japan owing to the outbreak of its long and bloody civil war from 1861 which effectively diverted its attention from foreign expansionism for some time.

All that the Western powers could do in Japan, given this background, was to mount a few small scale naval expeditions which fired on Japanese ports

and had the effect of galvanising a section of the anti-Shogunate nobility into mobilising for far-reaching political and structural change. In the summer of 1863 a British fleet shelled Satsuma han and burnt to the ground one third of Kagoshima, its main port. In 1864 the han leaders of Choshu closed the Shimonoseki Straits to foreign shipping and in punitive retaliation a joint force of the British, Dutch, French and Americans shelled Choshu heavily. The superior firepower of the Western imperialists convinced the leaders of Satsuma and Choshu that Japanese capitulation was inevitable unless Japan modernised militarily, a necessary condition for which was industrialisation, which lay behind the West's apparent invincibility. It was also clear to them that industrialisation and modernisation was not possible within the existing feudal political and economic structure.

In the decade 1858-68, the Shogunate too recognised the need for modernisation and on the basis of foreign loans, set up dockyards, ironworks and other industrial plants modelled on western lines. Warships and merchant vessels were purchased from abroad and envoys were sent to study foreign conditions. The lords of Satsuma and other tozama han also invested in iron foundries, mining enterprises and shipyards.

With the unrestricted entry of manufactured goods from abroad after 1858, there was displacement of the Japanese producers of textiles and some household goods, causing unemployment. There was a steep rise in the prices of goods in response to demand abroad including in prices of raw silk, rice, tea etc. Thus the domestic consumers of these goods as well as textile producers faced more difficult times, though a section of the well to do rural producers benefited from increased export demand.

The number of peasant revolts increased markedly during this period. A total of 86 cases of peasant uprisings in different parts of the country are recorded during 1860-67 compared to 71 during the period 1844-59 according to Kokusho Iwao, and 600 during the 265 years of Tokugawa rule.

The Emperor had emerged as a focus of anti-Bakufu and patriotic feeling when, in an unprecedented action, he had refused to ratify the 1858 Unequal Treaty with the USA. 'Revere the Emperor, expel the Barbarian' became the rallying cry of those who thought in terms of political change. The Tokugawa had promoted Buddhism, so a revival of Japan's ancient Shinto practices was also associated with this movement.

Towards the end of 1867 both the old Emperor as well as the Shogun passed away from natural causes. This provided the opportunity for a shift in the locus of power without civil war. The heir to the Shogun was a minor and was persuaded to step aside for the nominal restoration of the young Emperor, in 1868, but real power passed to a group of noble statesmen of the erstwhile tozama han aided by able samurai and supported financially by the great merchant house like Mitsui. The reign of the new Emperor was termed Meiji, hence the term 'Meiji Restoration' to denote this event. The reign of the Emperor Meiji was to last from 1869 to 1912, a period which saw Japan emerge as an industrialising economy and an aggressively expansionist State recognised by the Western powers as a force to reckon with.

Check Your Progress 3

- 1) Discuss the indices of peasant discontent during the Tokugawa era.

.....
.....

During the Tokugawa era, the emperor was virtually power less and the Tokugawas were de facto rulers. The clans which had fought alongside Tokugawa in 1600 were known as the fudai. The tozama daimyos comprised the opposition in the Battle of Sekigahara. To maintain control over the daimyos, particularly the Tozamas, the Tokugawa Shogunate created a system known as Sankin Kotai so as to discourage revolt by the daimyo. This system indirectly accelerated the pace of economic development through an improvement in transport and communications and by developing the financial and the banking system. Agrarian productivity also rose from the mid-18th century with increasing cropped area coming under irrigation, more intensive use of commercial manures and labour and higher labour productivity. This increase in productivity coupled with the increasing proportion of post-rent-cum-tax to output retained by the landowners over time led to the prosperity of the well-to-do minority of the landowners who invested their surplus in agrobased processing and in setting up industries. There emerged in the village economic scene a new category of landed entrepreneurs called oyakata.

However, the majority of peasants operating medium and small farms could not reap the benefits of a declining land rent-cum-tax as a proportion of the rising agricultural output—especially rice. A marked rise in economic inequality within the agrarian structure led to peasant discontent, often manifested in peasant revolts. They formed a politically mobilisable force which supported the moves for a change in the old feudal order.

The impact of the West was also conducive to a change in the old feudal order. Unlike in the case of China and India, the Western powers were unable to convert Japan into their colony. The USA was the first country to make an attempt to penetrate Japan commercially in 1853. The other powers to follow suit and impose a series of Unequal Treaties were Holland, Russia, Britain and France. These treaties led to the opening up of the Japanese economy leading to the unrestricted entry of manufactured goods from abroad after 1858 causing domestic unemployment and export of raw materials and agricultural goods leading to a steep rise in the domestic prices. Peasant unrest, as a result, gathered momentum. The Tokugawa was the Japanese partner to the Unequal Treaty. The Emperor, who virtually enjoyed no power in the Tokugawa era generated massive patriotic feeling by refusing to ratify the 1858 Unequal Treaty with the USA. In 1867, both the old Emperor and the Shogun passed away leading to a nominal restoration of the Emperor with the real power at the hands of the tozama han. The reign of the new Emperor was termed Meiji, hence the term Meiji Restoration.

5.7 KEY WORDS

Bakufu : military dictatorship.

burakumin : 'outcastes'.

Cho : unit of measurement of area of land equalling 2.45 acres.

Chonin : 'merchants'

daimyo : 'overlord' or 'noble'

fudai : clans which had fought alongside Tokugawa in the Battle of Sekigahara, in 1600. Another meaning of fudai is farm servants having tied or bonded status working virtually as slaves of the richer households.

genin : farm servants working for life in various forms of tied or bonded status employed by the *jiyushi*

- goyokin** : forced loan which the aristocracy often exacted from the chonin
- han** : a territorial unit under the control of a hereditary ruling clan led by a noble, the daimyo
- hatamoto** : troops maintained by the Shogunate
- hinin** : 'non-people' : they were considered to be sub-human.
- jinushi** : section of the peasantry holding substantial land for cultivation. They enjoyed a hereditary right of occupation and cultivation of land.
- jōka-machi** : 'castle-town' where the daimyo with his Warriors resided
- ko** : artisans and manufacturers
- koku** : unit of measurement of physical volume of rice equalling 4.96 bushels
- kosaku** : section of the peasantry comprising occupiers of medium to small and very small holdings of land
- kuge** : nobles of ancient lineage, based in Kyoto
- nago** : customary tenants. A large number of kosaku took some land from the jinushi as nago.
- no** : peasants
- oyakota** : landed entrepreneur who invested their surplus in agro-based industries and manufacture of textiles
- ronin** : wandering masterless samurai during the Tokugawa Peace
- samurai** : 'armed warriors'. They were maintained by the daimyo
- sankin kotai** : A system of 'alternate attendance' instituted by the shogunate to maintain control over the great daimyo, particularly of the tozama hans.
- shi** : samurai
- sho** : merchants
- Shogunate** : Regency
- Tokugawa** : de facto ruler of Japan, the actual Emperor being powerless.
- tozama** : 'outside' : the clans which opposed Tokugawa Iyeyasu in the Battle of Sekigahara in 1600

5.8 SOME USEFUL BOOKS

- Halliday, J. 1975 : *A Political History of Japanese Capitalism*, Pantheon Books, New York.
- Moore, Barrington, 1973 : *Social Origins of Dictatorship and Democracy* (Penguin University Books).
- Norman, E.H. 1975 : *Japan's Emergence as a Modern State* in J.W. Dower (Ed.) *Origins of the Modern Japanese State : Selected Writings of E.H. Norman*. Pantheon Books, New York.
- Smith, T.C. 1959 : *The Agrarian Origins of Modern Japan*, Stanford University Press, Stanford.

5.9 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) Read sub-section 5.2.1 and answer
- 2) Read sub-section 5.2.2 and answer
- 3) Read sub-section 5.2.3 and answer

Check Your Progress 2

- 1) Read sub-section 5.3.1 and answer
- 2) Read sub-section 5.3.1 and answer
- 3) Read sub-section 5.3.1 and answer
- 4) Read sub-section 5.3.2 and answer

Check Your Progress 3

- 1) Read section 5.4 and answer
- 2) Read section 5.5 and answer
- 3) Read section 5.6 and answer
- 4) Read section 5.5 and answer



ignou
THE PEOPLE'S
UNIVERSITY

UNIT 6 SPECIFIC FEATURES OF THE JAPANESE TRANSITION TO CAPITALISM—AGRICULTURE AND INDUSTRY

Structure

- 6.0 Objectives
- 6.1 Introduction
- 6.2 Abolition of the Feudal Agrarian Structure from Above
 - 6.2.1 Nature of the Restoration Process
 - 6.2.2 Abolition of the **Han** and the Feudal Tenures
 - 6.2.3 Rehabilitation of the **Daimyō** and **Sanzarai**
- 6.3 The New Agrarian Settlement : 1873-78
 - 6.3.1 Basis of Estimation of the Land Tax
 - 6.3.2 Distribution of Net Output among Social Groups and the Contribution of Land Tax to Revenues
 - 6.3.3 Social Consequences of the Land Settlement of 1873
- 6.4 The Supply of Labour and Scale of Production
 - 6.4.1 Small-scale Production in Agriculture
 - 6.4.2 Combination of Agricultural Cultivation with Sericulture and Hired Labour
- 6.5 The Agricultural Growth Debate and Import Dependence
 - 6.5.1 Initial Estimates of Agricultural Growth During 1873 to 1922
 - 6.5.2 Nakamura's Revised Estimates and their Implication
 - 6.5.3 Imports of Food and Primary Sector Raw Materials from Japan's Colonies
 - 6.5.4 Historical Reassessment of Early Japanese Industrialisation
- 6.6 Let Us Sum Up
- 6.7 Key Words
- 6.8 Some Useful Books Articles
- 6.9 Answers/Hints to Check Your Progress Exercises

6.0 OBJECTIVES

This unit will give you an idea of :

- the social consequences of increasing land concentration after the Land Settlement of 1873;
- output and productivity rise in Japanese agriculture and its contribution to development—the debate between different schools;
- the role of the colonies relative to domestic agriculture.

6.1 INTRODUCTION

The question of the part played by the rural sector in industrialisation has been of sustained interest for economic historians and students of development. A prior transformation of agriculture in a more productive capitalist direction has been put forward often as a necessary condition for industrialisation. Yet Japan did not have a capitalist transition in agriculture after the Meiji Restoration in the way Britain had. As you will recall Britain underwent a capitalist transition with the 16th to 18th century 'enclosures' and the associated cropping and technical changes accompanying larger-scale production by capitalist farmers hiring workers.

There are two main ways in which the rural sector can contribute to the development process. First through the transfer of surplus, in financial terms via taxation and terms of trade movements, which is matched in real terms by net sale of foodgrains and raw materials to the non-agricultural sector. Second, through the supply of labour for an expanding non-agricultural sector.

Many scholars of Japan have maintained in the past that Japan was unique in successfully meeting the requirements of early industrialisation from 1873 to 1922 even without a capitalist transformation and on the basis of small-scale production. They argued that this was possible because agricultural production had not reached its potential and the growth rate of output could be quite high. But research over the past three decades by economists dissenting from this view has cast serious doubt on the success of Japanese agriculture in meeting the foodgrains and raw materials needs of industrialisation.

These authors have pointed out that on the contrary Japan relied increasingly on its colonised territories for foodgrains and raw materials and this was because the Japanese rate of growth (of agriculture as well as the total domestic product) was in fact considerably lower than earlier estimated.

This unit will focus on this very interesting debate which is leading to a reassessment of the agriculture-industry relationship in early Japanese industrialisation.

6.2 ABOLITION OF THE FEUDAL AGRARIAN STRUCTURE FROM ABOVE

6.2.1 Nature of the Restoration Process

In order to understand the trends of concentration of land ownership and increase in tenant farming (as distinct from owner farming) which were both very marked from 1873 to 1914, it is first necessary to understand the character of the Meiji Restoration.

The Meiji Restoration of 1868 represented a 'revolution from above', carried out by the most active and enlightened section of the former feudal aristocracy itself, supported by the rich merchants of Osaka. It did not represent a 'revolution from below' where the oppressed peasantry rises en masse to throw off the yoke of feudal burdens and is led by the capitalist producers who similarly chafe under feudal restrictions on mobility of capital and labour. Such 'revolutions from below' took place in France from 1789 and to some extent in England during the Civil War of 1640-60. In Japan, however, the merchant capitalist class never asserted itself politically against the feudal aristocracy and therefore never led a popular movement for political change. On the contrary as we have seen earlier, the **chonin** allied themselves with the progressive **daimyo** and **samurai** who wished to rapidly industrialise Japan to counter the threat of foreign domination.

This does not mean that peasant uprisings were not important in toppling the old feudal regime. In frequency and severity the peasants' revolts were very important, and their frequency rose tremendously during 1858-1868. But the demands and interests of the peasantry who contributed to the overthrow of the Bakufu were not important to the leaders, who may have represented radicalism compared to the **shogunate**, but who were at the same time very conservative from the point of view of a broad-based democratic movement.

They rode to victory on the back of the support of the peasant revolutionaries and promised the latter that the Shogunate's land would be redistributed to them.

Once in a position of power, however, this now conservative leadership of ex-daimyo and ex-samurai administrators, proceeded to implement a land settlement which favoured their own interests, led to rapid rehabilitation of the samurai, and increased the landed estates of the Emperor. This was done at the expense of the ordinary peasants. The latter were not entitled to vote in the new system or to hold public office, as there was a stiff qualifying property ownership requirement. The details of the new settlement and its results are given below.

6.2.2 Abolition of the Han and of Feudal Tenures

The new government drew its statesmen and administrators from the han leaders of Satsuma, Choshu, Hizen and Tosa and from the samurai, and functioned with support from the merchants. This coalition set about dismantling feudalism from above. In 1869 the legal equality of all classes was proclaimed, and the clans were asked to surrender their hans to the government. The daimyo and samurai who thereby lost their rice rents, were allotted annual pensions by the government amounting to half of their estimated previous income.

Freedom of cropping was allowed, where previously it had been decided by the daimyo's or shogun's officials. Individuals could acquire property rights in land. The barriers to movement of goods and people by way of the tolls and taxes at entry point to the various hans were swept away. However a new agricultural taxation system required a fresh survey of area cultivated and of yields, and this required time. A new tax system came only in 1873. In the mean time the government faced considerable financial difficulties. In 1868 its expenditure was Y (Yen) 25 million while revenue was only Y 3.7 mn. Despite borrowing from Mitsui and other domestic and foreign merchant houses, a deficit of Y 16 mn remained. In 1869 too the deficit was about half of the total expenditure after taking all borrowing into account. The government had to resort to printing money and as much as Y 48 mn was printed in these two years. A violent inflation resulted, which hit all wage earners and fixed income earners hard.

At the same time it became clear that the new government had no intention of redistributing land to the peasants. The number of peasant revolts at 91, in the decade after 1868 in fact was even higher than during the preceding fifteen years. (Not all peasant agitation was on account of worsening economic trends. Peasants showed their superstitious and obscurantist side too on occasion by revolting against the legalisation of Christianity and abolition of the burakumin's near 'untouchable' status.) There was a feudal rebellion in Saga han in 1874 and a more serious armed uprising in Satsuma in 1877. On the whole however the major change of abolition of the han was accomplished remarkably smoothly and without a prolonged civil war.

6.2.3 Rehabilitation of the Daimyo and Samurai

While the daimyo were completely cut off from their base in landed property, the government made sure they would emerge as the dominant financial power in society, next only to the **chonin**, by paying generous compensation in interest bearing bonds, which was then legally recognised as the permissible form of reserves for a new system of 'national banks' which were set up. In short the daimyo's feudal rent was capitalised (at a rate of interest of 6 to 8 per cent) and the capitalised value paid as bonds. For

worth 4,200 yen, then half of this or 2,100 yen was first paid as annual pension, which from 1877 was compulsorily capitalised say at 7 per cent rate of interest, to give 30,000 yen worth of bonds (multiple of $100/7$ or 14.3 times the annual income).

Thus from being territorial magnates, the daimyo became financial magnates. They could invest their wealth and become shareholders in the banking system.

Samurai were much more numerous—there were over 2 million of them in 1868 and their rehabilitation was a major problem for the regime. Samurai ranged from the upper samurai next only to the daimyo in their income, to large numbers of ordinary men at arms. They too had the option of taking the capitalised value of their pensions in the form of bonds, which was made compulsory in 1877. Samurai also invested in banks, but the major avenues of their absorption were in the army and the police force. Grants of land or sales at nominal prices of land in Hokkaido, the northern most cold wind swept island of Japan, were made to the samurai to induce the settlement of this sparsely populated region.

The total value of bonds issued in stages to the ex-feudal classes was Y200 million, plus Y10 million paid in cash. This large compensation was ultimately financed by placing a heavy taxation burden on the peasantry, who thus had to buy their freedom from feudalism as well as contribute to industrialisation.

Table 6.1 : Commutation of Daimyo and Samurai Pensions to Bonds

Date/Period	Bond Value m.yen	Rate of Interest %
Samurai (1874-76)	16.565	8
Daimyo (1877)	31.412	5
Daimyo & Samurai (1872)	25.004	6
Daimyo & Samurai (1877)	108.243	7
Shinto Priests (1877)	0.334	8
Samurai	9.244	10
	190.802	
	20.109	mn. cash
	210.911	Total

Source : Norman 1975, p. 202

Immediately after the consolidation of the regime the leaders chose to set up a national banking system on the U.S. model in 1872 rather than a central banking system on the European model which turned out to be an unwise decision. The monetary situation at that time was quite alarming as, apart from the Government's own large issues of money to finance its deficits, more than 1500 varieties of han notes were still in circulation. A unified modern monetary system had to be built out of this chaotic situation; in 1872 the government's revenues at 33 m yen met only a little more than 60 per cent of its expenditures, and the amount of Government notes in circulation rose to over 73 million yen that year.

Under the Regulations of 1872, national banks could be set up by depositing a part of their reserves in gold and the remainder as paper money against which the government issued bonds. The banks could then issue their own notes which were convertible in gold. This system could not work as long as

merchants found it profitable to keep converting the issuing national banks notes to gold and drained the banks of their reserves. Under the revised regulation of 1876, the requirement of gold reserve and the convertibility clause were removed and the national banks were empowered to issue notes against only the security of Government paper money obtained against bonds deposited with the treasury. This experiment was enthusiastically taken up by the ex-feudal classes who were being compensated in Government bonds, for they could now use these bonds to become shareholders of the national banks. That probably was the main idea of the government in framing such regulations.

Between 1876 and 1880, as many as 148 national banks were formed and they made large note issues. The banks were formed by persons of no previous business experience and were badly managed, but they served their main purpose of financially entrenching the ex-daimyo and Samurai into the centre of a modern system though this was still in an experimental stage. The banking experiment converted the ex-feudal groups into a financial oligarchy, and did so at the expense of the ordinary wage-earners and small peasants who faced the brunt of the violent inflation which resulted.

Table 6.2 : Distribution of Shareholding in the National Banks in 1880

Class/Group	Share Value million yen	Per cent to total
Ex-daimyo and kuge	18.572	44.1
Samurai	13.417	31.9
Commoners, of which		24.0
a) Chonin	6.252	14.85
b) Rich farmers	1.452	3.45
c) Artisans	0.502	0.12
d) Others	2.367	5.62
	42.111	100.0

Source : Norman 1975, p. 207

It can be seen from the above data that the ex-daimyo, kuge and samurai held 76 per cent of shares in the banking system.

Check Your Progress 1

- Briefly describe the character of the Meiji Restoration. Discuss in this context the change in the economic and social status of different groups in Japan.

.....

.....

.....

.....

.....

- Why did a violent inflation result in Japan soon after the Meiji restoration?

.....

.....

.....

.....

- 3) What role did the rehabilitation of the daimyo and samurai play in the setting up of a national banking system in Japan?

.....
.....
.....
.....
.....

6.3 THE NEW AGRARIAN SETTLEMENT : 1873-78

6.3.1 Basis of Estimation of the Land Tax

In 1872 a cadastral land survey was carried out and the area under cultivation was recorded as 4.50 m.chō compared to the pre-1868 estimate of 3.23 m.chō. (Evidently the increase by nearly 40 per cent was not real, but reflected the fact that a substantial part of the under-reporting of cultivated area in the late Tokugawa, was eliminated by the survey.) The annual net output of agricultural products was estimated (by deducting from gross output, non-labour production costs) and an average of five years' net output was valued at prevailing prices. This estimated output value was then capitalised at between 6 to 7 per cent interest rate to give the land value. In other words, about fifteen times the value of annual net output was taken as land value. A tax in cash amounting to 3 per cent of this land value was then imposed on landholders.

Certificates of land ownership or *chiken* had been previously distributed to the farmers. The main feature of the new system was that the land tax was payable in cash and not in kind as a share of produce, as earlier. Secondly the estimated land tax was very high and provided no relief to the peasantry as compared to the Tokugawa rent-cum-revenue. The main reason was that a) the scope of taxation was widened since a lot of land was brought within the net through an up to date survey. Even though most of this unearthing of concealed land apparently affected the *jinushis* who had done most of the under-reporting, they passed on the increase in tax to their tenants. b) The estimate of net output was on the high side in not making adequate allowance for cost of production. Moreover, the theoretically correct basis for estimating land value is to capitalise the surplus obtainable from a unit of land. The 'net output' however is larger than 'surplus' since it does not exclude labour cost as surplus does. Hence the land value was overestimated since it capitalised net output, and not surplus.

6.3.2 Distribution of Net Output among Social Groups and the Contribution of Land Tax to Revenues

The rapid inflation which accompanied the period of the new land tax (1872 to 1876) benefited the landlords greatly, as they received the same rent from their tenants as before in kind and could pay a smaller and smaller fraction of the kind rent after sale as cash tax to government, keeping the balance for themselves. As they enriched themselves the *oyakata* in rural areas went in for investment in agro-based processing, set up silk filatures and weaving establishments, and also bought shares in urban industry which was just beginning to develop. An estimate of the share of agricultural net output value accruing to the landlords shows a substantial rise compared to the pre-1872 situation by 1876.

Table 6.3 : Distribution of Agricultural Net Output among Social Groups

Period	Percentage Share of Agricultural Net Output Value to		
	Landlords	The State	Tenants
Tokugawa	28	35	35
Tax Reform : 1873	34	34	32
Tax Reduction : 1876	38	30	32

Source : Adapted from Norman, 1975, p.257.

The last entry in the above table, 'Tax Reduction 1876' requires explanation. Such was the distress caused to small owner cultivators by the high rate of tax, and such was the agitation against it that the Government was forced to reduce the tax to two and half per cent of land value in 1876. This gave some relief to the small owners and benefited the landlords even more, while leaving the situation of tenants unchanged. The specific consequences of the high rate of land tax in leading to loss of land for small owners is discussed in more detail in Sub-section 6.3.3.

In the first fifteen years of industrial development in Japan from 1873, the land tax contributed over 76 per cent to total Government tax revenues and in the next fifteen years up to the turn of the century it contributed 42 per cent of total revenues. Thus it is perfectly correct to say that the agricultural surplus was the main source of mobilisation of resources for the government. The government in turn, was the main investor particularly in the new infrastructural and producers goods industries, so the land tax provided an important means of financing early industrialisation. However we must not underestimate the importance of the other main method of raising resources, which was less visible and direct but very potent, and which caused as much of a burden on the poor: that is inflation, arising from deficit financing and credit financing of Government's expenditures.

Table 6.4 : Contribution of the Land Tax

Period	Land Tax (000 yen)	Total Tax (000 yen)	Per cent of Land Tax to Total Tax
1873-1882	657,431	532,079	80.9
1883-1892	651,794	407,706	62.6
1893-1902	1,035,533	415,584	40.1
1903-1912	2,844,619	755,598	26.6
1913-1922	5,659,549	739,594	8.8
1923-1932	8,431,138	681,624	8.1

Source : Halliday 1975, pp 48-51, Calculated from annual series.

6.3.3 Social Consequences of the Land Settlement of 1873

We have referred to the violent inflation which marked the Government's early efforts to deal with its fiscal deficits, combined with the operation of the system of national banking designed to put the ex-feudal classes in a commanding financial position. The index of rice prices doubled between 1877 and 1881. This gave a bonanza to the landlords and benefited the medium producers, but the poorer farmers who were also partly dependent on wages, and the labourers lost out because on balance they had to purchase food on the market.

Table 6.5(A) : Index of Rice Prices—Inflationary Phase (Base 1873=100)

Year	Index
1873	100
1875	149
1877	111
1879	166
1881	221

Source : Norman, 1975

From 1882 however there was a change in Government's policy and on the recommendation of Finance Minister Matsukata, it was decided to switch over to a system of central banking and also undertake deflationary contraction of the economy. Accordingly the Bank of Japan was set up in 1882 to function as a central bank, and the national banks were required to transfer their reserves to the Bank of Japan. The inconvertible paper notes of the National Banks and of Government were rapidly withdrawn from circulation and replaced by a much smaller value of Bank of Japan notes, issued against a reserve of precious metals and made convertible from 1886. Money supply fell from 153 mn yen in 1881 to 123.6 mn yen in 1885. The resulting deflation was as violent as the earlier inflation had been.

Table 6.5(B) : Index of Rice Prices—Matsukata Deflation (Base 1873=100)

Year	Index	Year	Index
1881	221	1885	138
1882	184	1886	125
1883	131	1887	103
1884	110	1888	105

Source : Norman 975 p. 251.

It is against this background that the effects of the new land tax have to be assessed. For the small owners who were given the *chiken* and along with it the obligation to pay tax in cash, the burden was already heavy owing to their small resources, and with the Matsukata deflation they faced ruin. The landlords had large surpluses by way of rice rents and deflation simply squeezed their surplus, whereas for the small owners it became a question of survival since they had to cut down their subsistence to pay the tax. Many, thousands of them could not succeed in paying tax, and the government seized their land and sold it by auction in order to realise the arrears of tax.

Between 1883 and 1890, as many as 367,744 small farmers were forced to sell part of their land. The total tax arrears were 114,200 yen and the area seized and sold, 115,838.5 acres. Thus the unpaid tax per farmer was only 30 yen (equal to 0.3 yen), a negligible amount. The value of their land which was sold however was 4.944 million yen, or nearly 50 times the tax arrears. The people who bought this land were the landlords and merchant creditors, and for them the price was cheap at less than 50 yen per acre. The whole procedure amounted to a confiscation of the assets of the weakest and poorest farmers and transfer at cheap rates to the well-to-do. It greatly increased the concentration of land ownership in rural Japan and reduced more and more owner-farmers to part-tenants.

Apart from government sales of peasant lands, small farmers also lost land to creditors to whom they had mortgaged this land against loans. This was the beginning of a continuous trend of increasing concentration of ownership, combined with persistent small-scale of operation (since those who acquired more land leased it out in small parcels) and the growing importance of landlord-tenant disputes.

There was a very large rise by 3,650 times in the land allotted to the Emperor's estate between 1882 and 1890, as part of a conscious State policy of building up the Emperor as the supreme authority to whom every Japanese owed unquestioning loyalty. This also represented another form of a deprivation of the peasantry on the basis of whose support, the Meiji Restoration had been accomplished. The Emperor became the largest parasitic landlord in Japan.

Table 6.6 : Size of Emperor's Estates (cho)

1882	1,000
1886	31,000
1889	1,130,000
1890	3,650,000

Source : Haliday 1975, p. 44.

Note : 1-cho = 2.45 acres.

By 1889 the **total** taxable arable (cultivated) land area in Japan was 5.03 mn. **cho**, so the Emperor's estates were at least 15 per cent of total area.

Check Your Progress 2

- 1) How was the net output value capitalised to obtain the land value in 1872? What is the theoretically correct basis for estimating land value?

.....

- 2) What was the main source of the Japanese government's resource mobilisation? How did the government invest these resources?

.....

- 3) How did inflation and the national banking system put the ex-feudal classes in a commanding financial position?

.....

- 4) Briefly assess the social and economic consequences of the new land tax (1873) in Japan during the 1880's.

.....

6.4 THE SUPPLY OF LABOUR AND SCALE OF PRODUCTION

6.4.1 Small-scale Production in Agriculture

Japanese agriculture did not see a capitalist transformation, such as occurred in England or in France before and concurrently with their industrialisation. By capitalist transformation, we refer to a situation where most of production is on the basis of employment of hired labour for profit in large-scale farms with investment in improvement of techniques.

In Japan although the extent of concentration of ownership of land rose, so that the average size of owned holding got bigger, the actual units in which land was cultivated not only remained small but became smaller over time, for the big land owners leased out land in small parcels to many petty tenants. The tenants worked the land with their own labour and that of their family members using their own equipment although sometimes the landlord provided equipment as well. They paid rent in kind as a share of the crop, and a half-half share to landlord and tenant was common for rice-growing land, but the rent could often go up to 60 per cent of gross output.

Such a system of small-scale production was no doubt suited to Asian conditions where irrigated cultivation of rice, the main staple, had a history of many centuries with empirically tested practices for obtaining maximum yields. It is generally supposed that small-scale tenancy of this type is not conducive to rapid technical change even if the latter is feasible (in the sense of a new technology package being available). This is because the tenants are too poor to invest on their own after paying half the crop as rent; while the landlords who in any case obtain a high rental income without investing anything in agriculture and merely because of a legal title to property, would rather use their surpluses in other activities yielding profit such as agroprocessing, trade, small-scale industry, etc.

There has been a school of writers on Japan's industrialisation, who have maintained that the Meiji landlord was an exception. Since, according to their estimates, Japan had quite a high rate of growth of agriculture, they argue that this came about through larger applications of fertilisers and labour i.e., more intensive cultivation, and the Meiji landlord took an active role in disseminating more productive cultivation practices to their tenants. On this view, small-scale tenancy such as prevailed in the Meiji era, did not act as a disincentive to achieving rapid growth through productivity rise, for the landlords substituted for capitalists.

However this entire perspective has been challenged by other writers who have argued that the rate of growth of agriculture (and hence also of gross domestic product) during the Meiji era had been grossly overestimated in the past. So important is the agricultural growth debate that we take it up for detailed discussion in Section 6.5.

6.4.2 Combination of Agricultural Cultivation with Sericulture and Hired Labour

In the Meiji era of early industrialisation there was no absolute decline in the number of workers in the rural sector although a relative decline (as a proportion of all workers engaged in the primary sector, did take place. Agriculture, forestry and fishing employed 16 million in 1913 compared to 15 million in 1872, considering the occupied population. The percentage employed in the primary sector had dropped to 60.8 in 1913 compared to

84.9 in 1872. Thus the addition to the primary sector working population of 1872, found employment in the secondary and tertiary sectors during the next four decades.

Specific Features of the Japanese
Transition to Capitalism—
Agriculture and Industry

The specific feature of the occupations followed by the Japanese rural population during this period was the great importance of **sericulture**. The international trade situation in the 1870, favoured the expansion of exports of raw silk from Japan owing to a) the depreciation of silver, against gold and commodities, which was a worldwide phenomenon and made exports from Japan, which was on the silver standard, progressively cheaper for the gold-standard countries of the West; b) the outbreak of silkworm diseases in Italy, the main producer of silk in Europe leading to a vacuum in the supply of silkworm eggs and of raw silk which Japan was in a position to fill. Despite the lack of tariff autonomy, Japan did not face serious international payments difficulties owing to the expansion of exports in this phase, although her imports of machinery and minerals rose.

Silk production like cotton textile production requires a number of distinct stages, each of which can be carried on in rural areas and generates employment. Some farmers specialised in producing silkworm eggs. The silkworms were raised by other farmers on mulberry plants; at the next stage the pupae were harvested and the silk thread reeled in silk filatures, employing anything between 6 to 30 workers and run by the merchant capitalists or landlords. The silk thread was then woven into cloth in weaving sheds similarly employing a number of workers. Yet another group of workers engaged in the dyeing and finishing of the cloth.

Increasing numbers of rural farming household engaged in one stage or another of sericulture in addition to farming activities. This provided a valuable supplementary source of income (which became a main source for some of the families). It is estimated that production of silk employed as many as 5 million rural households by the end of the Meiji era (compared to less than 1 million employed in the organised factory sector). Exports of raw silk accounted for nearly 80 per cent of production throughout the period. The standardisation of output and quality control required for sustained exports to distant markets in the U.S.A. and Europe, was achieved through a number of measures. These included Government licensing of producers of silkworm eggs, setting up of model filatures employing the latest machinery and their popularisation, and financial control. This last, namely, financial control, was exercised via the Yokohama Specie Bank giving loans to the exporting concerns of the *zaibatsu*, which in turn through myriads of rural agents advanced money to the silk spinners and weavers while specifying the type and quality of product.

Japan thus developed a symbiosis of small to medium scale rural industry side by side with large-scale factories in urban areas, producing the same commodities. This system was of advantage to organised industry, for the rural workers were generally paid at lower rates. When demand expanded the supply could be quickly stepped up by drawing in larger numbers of part-farmers into silk production. On the other hand the burden of adjustment of recession and cutback in output could also be passed on to the rural producers, thus insulating the factory sector from fluctuations. The economists refer to it as a 'dual' or 'differential' economic structure which was peculiar to Japan among the industrialising countries, and came to characterise not only silk production but many other branches of light industry as well.

Labour organisations in industry were not permitted under a repressive 'Peace Preservation Law, and unionisation was very difficult owing to the

predominance of female labour in the textile factories in particular. It was the daughters of farmers who migrated to their towns seeking employment. The share of female workers to all workers employed, (in factories with over 10 workers and excluding government run ones) rose from 59 per cent in 1895-99 to 71 per cent by 1910-14. In the textile factories it was even higher at 80.1 per cent in 1909.

Check Your Progress 3

- 1) What do you understand by the term capitalist transformation of agriculture? Which are the countries that witnessed a capitalist transformation? What happened in the case of Japan? Was it suitable from the point of view of productivity?

.....

.....

.....

.....

.....

- 2) Briefly describe Japan's 'dual' economic structure. In what ways was this system advantageous to the organised industry?

.....

.....

.....

.....

.....

6.5 THE AGRICULTURAL GROWTH DEBATE AND IMPORT DEPENDENCE

6.5.1 Initial Estimates of Agricultural Growth during 1873 to 1922

The very crucial role played by agriculture in promoting early Japanese industrialisation is a fact which is not in dispute. There exists a controversy however, on whether Japanese agriculture did in fact succeed in meeting all the food and raw materials requirements of industrialisation through an adequate rate of growth of output; and whether it met the requirements of industrial expansion relatively painlessly in terms of the burden on the peasantry, or whether it did so substantially at the expense of the peasants. The answers to the two questions are closely related, for if the growth rate of Japanese agriculture in the Meiji era was in fact higher than the population growth rate, then *prima facie* for a given distribution of assets and income, the burden of financing industrial development on the peasants could not have been very onerous. On the other hand if the growth rate was low and fell short of or barely matched the population growth rate implying that productivity per capita did not rise, then the measures of heavy taxation and rapid price inflation and deflation we have discussed would have imposed a considerable burden on the peasants.

The initial estimates using the unadjusted official statistics of the growth performance of Japanese agriculture during the period 1878 to 1917, carried out by Ohkawa, and for 1881 to 1920 by Johnston, suggested a quite favourable rate of growth per annum of 2.4 per cent and 1.9 per cent respectively (Table 6.6), entailed in a more than doubling of output over the

period in the case of the first estimate and a 75 per cent rise in the case of the second. The labour force in agriculture over this period rose by only 10 per cent or so, implying a very substantial rise in productivity. It was argued by authors of the Ohkawa school that such a large rise in productivity was possible because of the existence of a technical 'slack' in Japanese agriculture before the Meiji era, in the sense of the feasibility of more intensive cultivation and higher yields, which could be realised after 1868 once there was freedom of cropping, free mobility of labour, and the beginning of state-sponsored agricultural research and extension work. It was also argued that the existence of small-scale tenancy and landlordism was quite compatible with rise in productivity because of the bio-chemical nature of the technical change (pure line selection of crops, more input of fertilisers per unit area) which can be undertaken on small areas unlike European type mechanisation; and because the Meiji landlord was an improvement minded, entrepreneurial landlord constantly advising his tenants on the best cultivation practices.

Table 6.6 : Index of Agricultural Output

Period	Ohkawa	Johnston	
1878-82	100	1881-90	100
1883-87	116	1891-1900	127
1888-92	140	1901-10	146
1893-97	147	1911-20	177
1898-1902	171		
1903-07	187		
1908-12	211		
1913-17	236		
Growth rate : (compound p.a.)	2.4 per cent		1.9 per cent

Source : Nakamura 1966.

This interpretation of the role of agriculture did not seem to fit with other facts, however. First, the scope for raising productivity very fast in the first two to three decades after 1868 would appear to be much less when it is recognised that a great deal of (officially unrecorded) productivity rise had already taken place in the century before the end of the Tokugawa era (Section 5.3). Secondly, the peasantry suffered loss of land and revolted repeatedly during the early Meiji, which is surprising if overall output expansion was indeed high.

6.5.2 Nakamura's Revised Estimates and their Implication

The initial view of the role of agriculture in the industrial development in Japan, which dominated studies in this area, received a severe challenge from the alternative estimates of agricultural growth put forward by J.I. Nakamura. According to the latter's argument, both the area under cultivation and yield per cho of crops were gross underestimates on the eve of the Meiji Restoration. The first cadastral survey of 1872 carried out by the new government uncovered quite a lot, but not all the under-reported area. Thus the total area under cultivation in 1872 was reported as 4.50 million cho compared to 3.23 million cho before 1868. Such a large rise of nearly 40 per cent could not have actually taken place in reality, and reflected rather a more accurate coverage of actually cultivated area. However the incentive to under-report area and yield for the big landowners (who also provided the

officials who kept the village-level records) continued since government had declared that it would carry out periodic resurveys and on that basis revise tax demand: in 1885 and 1889 further surveys were in fact carried out. The later surveys uncovered the remaining under-reported area, so that from the turn of the century the official statistics reflected reality on the ground with only small margins of error. The earlier data for the 1870s and 1880s however required upward revision.

On the basis of adjustments to the official data undertaken under specific assumptions, Nakamura obtained an index of agricultural production between 1873 and 1922, showing a less than 50 per cent rise. The mean compound growth rate per annum over this period works out to 1 per cent (with a maximal rate of 1.2 per cent and a minimal rate of 0.8 per cent depending on the assumptions made). This barely kept pace with the population growth rate. The data on per capita consumption of rice shows near stagnation and tends to confirm this output estimate.

Table 6.7 : Nakamura's estimate of agricultural production

Nakamura's Adjusted Index of Agricultural Production		Per Capita Consumption of Rice per Annum, (koku)	
1873-77	100.0	1880-84	0.80
1878-82	102.6	1885-89	0.93
1883-87	105.9	1890-94	1.01
1888-92	109.2	1895-99	0.95
1893-97	112.6	1900-04	1.05
1898-1902	118.1	1905-09	1.07
1903-07	123.9	1910-14	1.07
1908-12	131.6	1915-19	1.13
1913-17	137.6	1920-24	1.10
1918-22	144.7	1925-29	1.14
		1930-34	1.08
		1935-39	1.06

Compound growth rate : 1 per cent per annum

Source : Nakamura 1966, Allen, p. 217.

Nakamura's argument is a reasonable one and earlier authors have been obliged to rework their estimates by undertaking some adjustments though not to the same degree. The resulting statistical compromise is given below from Ohkawa's revised growth rates in the light of Nakamura's criticisms.

Table 6.8 : Annual Growth Rate in Agriculture

Year	Total Output	Total Input	Total Productivity
1880-1900	1.6	0.4	1.2
1900-20	2.0	0.5	1.5
1920-35	0.9	0.5	0.4
1935-45	-1.9	-0.9	-1.0

Source : Ohkawa 1979, p. 88.

According to Nakamura the above estimates are still overestimates for the period 1880-1920. Indeed it is difficult to see why Japan should have become

a net importer of food to an increasing degree after 1895, if her domestic agriculture was indeed growing faster than the population, given the date on near-stagnation in per capita consumption of food. The next section discusses the question of import-dependence by Japan on her colonies.

6.5.3 Imports of Food and Primary Sector Raw Materials from Japan's Colonies

Japan launched an aggressive overseas expansion on the Western imperialist model vis-a-vis the Asian mainland, within two decades of consolidation of the Restoration. Victory in the Sino-Japanese War of 1893-95 brought her Formosa (Taiwan) as a colony and effective control over the Korean peninsula. Taiwan was actively settled with State help by Japanese immigrants and was developed as a source of rice and sugar for Japan. Korea was similarly increasingly important as a source of rice imports and soon outstripped Formosa as a more important supplier. Whereas Formosan rice exports to Japan did not involve lowering of the consumption of the ethnic Chinese-speaking colonised people because productivity was also rising, in Korea it was otherwise. From exporting 11.4 per cent of its production of rice in 1912 to the metropolis, Japan; by 1932-36 Korea was forced to export 50 per cent of its production and this involved a fall in the food availability and caloric intake of the colonised Korean people. Thus Japan ran import surpluses with its colonies (by importing more than it exported), which she had no difficulty in paying for as she taxed the Koreans (after 1910) and Taiwanese at the same time. In effect, to pay tax the colonies had to export more than they imported and they got no command over foreign exchange earned from export surplus. This indeed is the classic pattern of colonial exploitation, to which India was subjected by Britain, for example, for an even longer period. This you have already studied in Block 1 of EEC-02, in the nature of unilateral transfers.

Table 6.9 : Per cent Distribution of Total Rice Imports into Japan From

Year	Korea	Formosa	Other	All
1911-15	24	20	56	100
1916-20	37	18	45	100
1921-25	47	17	37	100
1926-30	57	21	22	100
1931-35	65	30	5	100
1936-38	63	35	2	100
Per cent of Rice Exports to Rice Production in Korea		Caloric Intake per Capita in Korea		
1912-16	11.3	2133		
1911-21	17.3	2206		
1922-26	30.2	2033		
1927-31	41.9	1924		
1932-36	51.4	1812		

Source : Johnston 1953 51,54 and Shuh 1978.

It may be seen that Korea and Formosa up to the end of the first War supplied around at least one half of Japan's rice imports but by the inter-war period were together supplying 98 per cent of the much higher level of imports.

How important were net food imports compared to Japanese domestic

low levels of around 5 per cent of imports relative to home production of rice, the proportion rose steadily until it was 20 per cent in the period 1935-37 (Table 6.10).

Table 6.10 : Rice Production and Imports : 1880-1937

Period	Production mn. koku	Net Imports mn. koku	Per cent of Net Imports to Production
1880-84	29.96	- 0.18	- 0.6
1885-89	36.58	- 0.74	- 2.0
1890-94	40.36	+ 0.37	+ 0.9
1895-99	39.21	+ 1.15	+ 2.9
1900-04	44.64	+ 2.74	+ 6.1
1905-09	47.58	+ 3.18	+ 6.7
1910-14	51.17	+ 2.96	+ 5.8
1915-19	56.89	+ 4.18	+ 7.3
1920-24	56.34	+ 5.91	+ 10.5
1925-29	59.45	+ 10.01	+ 16.8
1930-34	62.23	+ 10.80	+ 17.3
1935-37	63.71	+ 12.46	+ 19.6

Source : Allen p. 217. The production data are official, hence are underestimates in the first decade 1880-1890.

This was accompanied by hardly any change in per capita rice consumption in Japan (indeed there is stagnation if the official figures for the decade 1880-90 are revised upwards to adjust for underestimation in Table 6.7), so it is very clear that in the absence of imports per capita consumption would have fallen. Japanese agriculture thus did not succeed in achieving food self-sufficiency in the process of industrialisation. Further Japan avoided serious balance of payments difficulties entailed in heavy food and raw material imports only through colonial exploitation, which enabled her to transfer food and raw materials as the commodity-equivalent of tax imposed (in excess of expenditures) on the colonised people.

Not only foodgrains, but other primary sector products of mining (iron ore, minerals) which were of crucial importance for Japanese industrialisation were also imported from the mineral rich region of northern Korea and Manchuria (northern China) over which Japan acquired control after the first War and seized officially in 1931. This will be discussed further in Units 7 and 8.

6.5.4 Historical Reassessment of Early Japanese Industrialisation

The role of agriculture in Japanese industrialisation and indeed the entire experience of industrial development in Japan require critical reassessment today and the final word has not been said yet. Traditional analyses which have ignored the contribution of the Japanese colonies, have presented a very favourable interpretation of successful transition to capitalist modernisation in Japan as a self-contained and independent phenomenon. The facts however, tell a somewhat different story. They suggest that the nature of the transition after 1868 in Japan which sacrificed the interests of the peasantry,

and led to increasing concentration of land under a landlord—petty tenant system, may well have hindered rapid growth of output quite apart from the social inequity that such a transition entailed. In consequence Japanese agriculture could not grow fast enough to ensure food self-sufficiency, even when demand was kept down through low rates of income rise for the poorer groups within Japan like tenants and labourers. Heavy import dependences without balance of payments problems was possible only through intensive exploitation of the colonised people of Taiwan, Korea and Manchuria. In at least the case of the Koreans it entailed falling consumption of basic food-grains and a drop of calorie intake below nutritional minimum levels so that Japan could be kept supplied with foodgrains.

Check Your Progress 4

- 1) What was the role played by agriculture in promoting early Japanese industrialisation? Discuss in this context, the contrasting viewpoints of traditional analysts and recent reassessments.

.....
.....
.....
.....
.....

- 2) What was the nature of the burden imposed on peasantry for financing early Japanese industrialisation in the late 19th century? Discuss the implications of Nakamura's revised estimates of the rate of agricultural growth in this context.

.....
.....
.....
.....
.....

- 3) What role did the Japanese colonies play in facilitating industrialisation of Japan?

.....
.....
.....
.....
.....

6.6 LET US SUM UP

In this unit you have read about the transformation of the Japanese agrarian structure after the Meiji Restoration of 1868 and how it contributed to Japan's industrialisation.

The Meiji Restoration, as you have read, represented a revolution from above. The merchant class allied themselves with the progressive daimyo and the samurai. These were the classes which primarily benefited from the Meiji restoration at the cost of the peasantry. While the daimyos were cut off from their base in landed property, the government compensated them generously

by capitalising their feudal rent and the capitalised value paid as bonds. Thus the daimyos could transform themselves into financial magnates. The samurai were also rehabilitated. This large compensation was financed by placing a heavy taxation burden on the peasantry who had to buy their freedom from feudalism.

A national banking system was set up on the U.S. model in 1872 which turned out to be an unwise decision. The money market was unorganised and fragmented and the government's fiscal deficit was enormous. Between 1876 and 1880 as many as 148 national banks were formed and they made large note issues. The ex-daimyo, kuge and the samurai held 76 per cent of shares in the banking system. Thus the banking experiment converted the ex-feudal groups into a financial oligarchy. However, the prevailing fiscal crisis and monetary chaos resulted in a rampant inflation and the poorer classes were ruined.

While inflation raged, in 1873 a new land tax was imposed which contributed to over 76 per cent of Government's total tax revenue (1873-1888). The land tax directly, and inflation, indirectly, contributed to the government's mobilisation of agricultural surplus which in turn was invested in infrastructural and industrial development. Thus agriculture played a crucial role in promoting early Japanese industrialisation. However, with the Matsukata deflation thousands of small farmers became indebted and were unable to pay land tax any further. Forcible seizure of land and then reselling to the well-to-do landlords accentuated the inequality in the distribution of agricultural landholdings in rural Japan. Simultaneously, the Emperor became the largest parasitic landlord in Japan. Japan did not undergo a capitalist transformation in agriculture unlike U.K. The big land-owners continued to lease out land in small parcels to many petty tenants. According to one school of thought, Japanese landlords played an active role in improving agricultural productivity and small-scale tenancy did not act as a disincentive to achieving rapid growth. However, another group of writers have challenged this viewpoint. According to the latter, in spite of increased agricultural productivity, Japan did not achieve self-sufficiency in foodgrains and raw materials production. This is the agricultural growth debate. While estimates of Ohkawa and Johnston, representatives of the traditional school, suggest a rather high rate of growth of agricultural output (their estimates were based on unadjusted official agricultural statistics), Nakamura's revised estimates show a much lower rate of agricultural growth.

In fact, one of the prime motives of Japan's aggressive overseas expansionist policies was the vital need for cheap imports of foodgrains, minerals and raw materials from her colonies like Formosa and Korea. Japan, like any other imperialist power, ran import surpluses with her colonies and achieved a steady rise of food imports from 5 per cent in 1895 to 20 per cent in 1935-37, without balance of payments difficulties as this import surplus embodied taxes transferred from these colonies.

Thus, it is not true, as traditional analyses assume, that Japan's capitalist development was a wholly independent and self-contained phenomenon. Its military prowess enabled Japan to overcome her deficiency in the production of foodgrain through transfer of foodgrains. Japan's dependence on her colonies as outlet for her exports was also quite significant as will be discussed in Unit 7.

6.7 KEY WORDS

6.8 SOME USEFUL BOOKS/ARTICLES

Allen, G.C., 1972, *A Short Economic History of Modern Japan*; George Allen and Unwin Ltd., London.

Halliday, J., 1975, *A Political History of Japanese Capitalism*, Pantheon Books, New York.

Johnston B.F. and J. Mellor, 1961, *The Role of Agriculture in Economic Development* in American Economic Review, Vol. 51 Sept.

Nakamura, J.J., 1966, *Agricultural Production and the Economic Development of Japan*.

Norman E.H., 1975, *Japan's Emergence as a Modern State*, in J.W. Dower (Ed) *Origins of the Modern Japanese State : Selected Writings of E.H. Norman*; Pantheon Books, New York.

Shuh, S.C., 1978, *Growth and Structural Change in the Korean Economy, 1910-1940*, Harvard University Press, Cambridge.

Ohkawa, K., 1979 *Aggregate Growth and Product Allocation* in a Ohkawa and M. Shinohara (Ed) *Patterns of Japanese Economic Development : A Quantitative Appraisal*.

6.9 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress

- 1) Read Sub-section 6.2.1 and answer
- 2) Read Sub-section 6.2.2 and answer
- 3) Read Sub-section 6.2.3 and answer

Check Your Progress

- 1) Read Sub-section 6.3.1 and answer
- 2) Read Sub-section 6.3.2 and answer
- 3) Read Sub-section 6.3.2 and answer
- 4) Read Sub-section 6.3.3 and answer

Check Your Progress

- 1) Read Sub-section 6.4.1 and answer
- 2) Read Sub-section 6.4.2 and answer

Check Your Progress

- 1) Read Sub-sections 6.5.1 and 6.5.2 answer
- 2) Read Sub-sections 6.5.1 and 6.5.2 answer
- 3) Read Sub-section 6.5.3 and answer

UNIT 7 THE JAPANESE STRATEGY OF INDUSTRIALISATION UPTO WORLD WAR I

Structure

7.0 Objectives.

7.1 Introduction

7.2 State Initiative in early Industrialisation

7.2.1 The Reasons for State Initiative and Direct Investment

7.2.2 Forms of State Intervention

7.2.3 The Banking System and its Role in Industrial Finance

7.3 Development of Heavy Industries and the Colonies

7.3.1 Japan's Resource Base and Economic Motives for Colonial Expansion

7.3.2 Progress of the Basic and Producer Goods Industries upto 1913.

7.3.3 Consumer Goods Industries and Foreign Trade.

7.4 Boom Conditions during World War I

7.4.1 Effects of the War on Industry and Trade

7.4.2 Price Inflation and the Rice Riots

7.5 Let Us Sum Up

7.6 Key Words.

7.7 Some Useful Books

7.8 Answers/Hints to Check Your Progress Exercises.

7.0 OBJECTIVES

After going through this unit, you will be able to:

- describe the role of the Japanese state in promoting early industrialisation;
 - analyse the economic motives behind Japanese colonisation;
 - discuss the change in production conditions in Japanese industry leading to the development of the basic and producer goods industries;
 - explain the effect of the boom conditions of the First World War and its impact on industrialisation, income distribution and the standard of living of the wage earners; and
 - discuss the reason for the failure of the boom.
-

7.1 INTRODUCTION

Japan pioneered the idea of active State intervention to promote modern economic development in the 19th century. This is an idea which is taken for granted today, but was new at that time when the dominant ideas were of *laissez-faire* (letting the economic system regulate itself without State intervention) and free trade.

As you will recall from Block 3, there was little that the Meiji leaders could do regarding free trade. The government was bound by the Unequal Treaties of 1858 with the imperialist powers, which did not permit Japan to raise tariffs against imports above 3 per cent (This level was so low that in effect Japan was an open economy.) But they could and did use the sovereign status of their country (as opposed to the colonial status of other Asians) to put the whole weight of State power behind building up a modern industry. The motive for rapid modernisation was initially defensive. There was, however, a very rapid transition to an offensive in the form of economic and military subjugation of weaker Asian countries.

This unit will discuss the strategy of early industrialisation upto the end of World War I in Japan. This initiative was taken up by the Meiji State. The admiration which Japan's economic and military successes against the Western powers evoked amongst

particular Asians who were colonised by Japan. A more balanced evaluation of early industrialisation in Japan is required which will take account both of Japan's positive achievements as well as the costs of these achievements both to her own population and to others.

7.2 STATE INITIATIVE IN EARLY INDUSTRIALISATION

It is true that Japan followed a capitalist path of industrial development. However, the Meiji state played an extremely significant role in promoting her industrialisation. Thus Japan's capitalism was state-promoted. In this section, we shall study the reasons and the forms of state intervention with special emphasis on the banking system and how it actively facilitated Japan's industrialisation.

7.2.1 The Reasons for State Initiative and Direct Investment

For the Meiji leaders the most urgent motive for industrialisation, after the Restoration, was the building of an adequate defence capacity to meet the threat of the Western powers. For this purpose it was necessary to invest, practically from a zero base, in Munitions, ship building, a modern communications system, and the basic industries required for defence production. Though the consumer goods industries already existed and were well organised, there was a need for inception of modern technology. The role of government in early industrialisation, therefore, focussed overwhelmingly not on light industry, but on defence-related heavy industry.

By their very nature, defence-related production and shipbuilding require large initial capital outlays, involve long periods of production, and can only be ensured a market through government absorption of most of the output through the demand of the defence services. These sectors of production could not conceivably be built in a short time through private investment alone. The private entrepreneurs in Japan at that time were the merchant capitalists engaged in trade and in financing the production of consumer goods, like textiles. To induce them to go in for defence-related production it was necessary for government to intervene directly, by

- setting up capacity,
- building model enterprises which private investors could emulate, and
- providing them purchase contracts which would guarantee a market. This was precisely the strategy followed by the Meiji State.

Owing to the focus on heavy industry, it has been argued that Japan followed a totally different path of growth in industry compared to the Western capitalist countries like England. There the 'leading sector' in the Industrial Revolution was textile and the machinery; producer's goods sectors developed later. Owing to the forced and hot-house development path in Japan, this pattern was reversed and most of additional investment after 1868 just went into the producer goods industries.

7.2.2 Forms of State Intervention

The first action of the Meiji State was to take over the shipyards, foundries and mines of the shogunate and daimyo. The intention was to modernise and enlarge them as the core of a new system of production. Thus the Nagasaki Iron Foundries, formerly owned by the Shogun, formed the core of the new **artillery works**; the Kagoshima Dockyards, started by the Satsuma **daimyo**, was enlarged and adopted to manufacture **ships of war**. By the early seventies the government was operating nine **mines** on a large scale (mining copper, gold, silver, iron ore and coal) as model enterprises. After 1880, mining development was mainly left to private enterprise.

Particular attention was paid to laying the foundations of a **mercantile marine**. Ocean-going ships were purchased from abroad and transferred to private entrepreneurs. Thus, a small firm had been founded by Iwasaki, an enterprising samurai, who had purchased three steamers from his daimyo and used them for coastal trade. When government needed ships in connection with an expedition to Formosa (Taiwan), it purchased these ships from abroad and entrusted Iwasaki's

lines set up with State help like the Kaisei Kaisha, were absorbed by Mitsubishi which, by 1875, owned 37 vessels.

During the 1877 Satsuma rebellion, government required Iwasaki's services again and the size of its fleet expanded considerably. In 1879 Mitsubishi started plying to Hong Kong and two years later to Vladivostok. These were the typical beginnings of Mitsubishi, one of the five giant monopoly houses, which were to dominate the economy during the next century. This case illustrates well the interpenetration and mutual accommodation of State and entrepreneurial interests so characteristic of Japan. (By contrast, during roughly the same period in India, the shipping activities of the Tatas and other West Coast shipowners were wiped out owing to the hostility of the British colonial government which passed laws specifying that all officers of ships plying from India had to be British).

The Meiji State passed the navigation Subsidy Act of 1896 under which Japanese shipowners received subsidies on the operation, in foreign trade, of ships of 1000 tons and above. Meanwhile, Mitsubishi had amalgamated with another group of small transport concerns called Kyodo Unyu Kaisha (United Transport Company) also started with State help. The amalgamated company, called Nippon Yusen Kaisha (NYK), was to become the chief Japanese shipping line. The state guaranteed dividends of 8 per cent on the company's capital and designated routes on which its ships were to run. With the help of the Navigation Subsidy Act the NYK soon started services to Australia, Europe and N. America before the end of the century.

Table 7.1
Growth of Mercantile Marine, 1873-1904

	Steamships (000 tons)	Sailing Ships (000 tons)
1873	26	8
1894	169	45
1904	797	227
1013	1514	828

Source: Allen, Short Economic History of Japan.

Apart from the mercantile marine, internal transport and communications required modernisation. The Meiji State was, in general, initially very careful in taking foreign loans. They had learnt from the experience of Turkey and Egypt which trapped in foreign debt, had the Western powers freely meddling in their internal affairs. It raised only two loans on the London market until the end of the century, and both were for building railways. The first loan, taken in 1867 for 3.75 million yen, was mainly for building Tokyo—Yokohama line; and the second for 10.7 mn. yen was raised in 1872 partly to cover the cost of paying pensions and partly to build a second railway line. Up to the 1880's the government was responsible for nearly all railway construction after which it was joined by a number of private firms. The railways were nationalised in 1906 when the total mileage reached 6,000.

The range of government direct investment upto 1885 was very wide. It set up the Senji Woollen Web factory for providing uniform cloth to the armed forces, started the Fukugawa Cement Works, the Shirakawa White Tile factory, and factories for producing sodium sulphate and bleaching powder. Model factories, equipped with the latest imported machinery, were set up for cotton and silk spinning; and modern spinning equipment was imported and sold to private enterprise on an easy instalment plan. Further, large numbers of skilled technicians and engineers were inducted from the West on contracts, their number reaching over 500.

Under the Transfer Law of 1880, a number of State enterprises were sold to private entrepreneurs on extremely favourable terms. The large element of subsidy involved may be gauged from the difference between what the government had spent to set up the enterprises and the transfer price paid by the buyers:

Table 7.2
Transfers under the Transfer Law of 1880

Enterprise	Transfer Price (000 yen)	Total Government Expenditure (000 yen)
Furukawa Cement Factory	250	468
Innai Gold Mine	75	195
Kosaka Mine	200	547
Shinagawa Glass Factory	80	189

7.2.3 The Banking System and its Role in Industrial Finance

The part played by the early system of national banking in rehabilitating the ex-feudal classes to make them one more financially powerful group, and the transition to a central banking system, have been discussed in Unit 6. Here we will focus on the pioneering role played by the developing banking system in financing rural and urban enterprises.

Today we are used to the idea of the active role played by an expanding modern credit system in promoting productive investment. But the conscious use of this policy was pioneered in Japan from the 1880s through the setting up of banks (under government support of the dividend rate) with definite functions of providing long-term investment in industry and agriculture.

After the establishment of the Bank of Japan as the central bank in 1882 the next step was the revision of the regulations of the Yokohama Specie Bank (established in 1880). This was necessary so that it could function as the chief foreign exchange bank of the country. The State provided one-third of the initial capital, and the Specie bank was closely supervised by it.

A large middle class prepared to invest directly in industrial shares did not exist at that time in Japan. Hence, the government proposed to mobilise private savings through the medium of bank debentures guaranteed by it. The Hypothec Bank of Japan was set up in 1896. It was empowered to (1) raise funds by issuing debentures, upto ten times its paid-up capital, and to (2) advance long-term loans, repayable in instalments over 50 years against the security of immovable property like paddy fields, other fields, forests and fishing rights. For the first 10 years the government guaranteed the banks to get dividends at 5 per cent. Under the Hypothec Bank, 46 prefectural Agriculture and Industrial Banks were established with the same purpose. The State exercised close supervision on the activities of these banks.

In 1900 the Industrial Bank of Japan was set up to provide long-term finance to industry with a similar government guarantee of its dividend and with the power to issue debentures upto 10 times its paid-up capital. This bank mainly gave credit to large-scale enterprises like iron and steel, chemical and machine-making, shipbuilding, and the public utilities.

With the acquisition of colonial territories after the Sino-Japanese and Russo-Japanese wars (discussed in section 7.3) the Government set up specialised banks for developing infrastructure and the agricultural and mineral resources of the colonies (particularly those in which Japan proper was deficient). These banks financed the activities of the *zaibatsu* (who undertook investment in large-scale colonial enterprise), as well as of Japanese settlers in the colonies.

These specialised banks, except for two, were modelled on the Hokkaido Development Bank, set up in 1899 to finance the settlement and growth of farming and other enterprise on Hokkaido, Japan's northern most island. The Bank of Formosa (Taiwan), set up in the same year, was exceptional in being empowered to issue notes and manage the colonial revenues, as well as trade. In Korea, the First Bank (Dai Ichi Ginko) initially acted as the note-issuing central bank. In 1909, the Bank of Korea (renamed the Bank of Chosen next year after the Japanese annexation of Korea) took over these functions of note-issue and handling the government account from the First Bank

In Korea a number of Hypothec banks were set up in 1906 on the Japanese model, and these were merged, in 1918, to form the Chosen Industrial Bank. The Oriental Development Company, formed in 1908, was also an industrial bank promoted by government with the function of financing industrial enterprise in the colony.

All these special banks were supported, through partial provision of their capital, by government. They acted under close government supervision, and invested cooperatively in enterprises of national importance.

Check Your Progress 1

1. What was the role of the Japanese government in promoting Capitalism?

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

2. How did the Japanese banking system promote industrialisation of Japan?

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

7.3 DEVELOPMENT OF HEAVY INDUSTRIES AND THE COLONIES

In this section we shall study why Japan pursued aggressive imperialist policies in Asia. Japan's industrial development and the role of foreign trade in Japan's industrialisation will also be discussed.

7.3.1 Japan's Resource Base and Economic Motives for Colonial Expansion

Apart from coal and copper, Japan lacked all the minerals required for building up a heavy industries production base. Consequently, import-dependence for essential minerals was large from the very beginning of the industrialisation process, even when the size of the modern manufacturing sector was very small. On the other hand, on the Asian mainland very near Japan, there were rich and varied deposits of minerals—in northern Korea, in Manchuria and in North China.

The speed with which the Japanese leadership turned from a building up of munitions, shipping and heavy industry for defensive purposes against the West, to an

economic motive of control over minerals and raw materials essential for industrialisation, was also a very important motive in Japan's colonial expansionism.

Within twenty five years of the Meiji Restoration, in 1893 Japan attacked China. This resulted in the Sino-Japanese war over the question of control over policy making in Korea.

A resounding victory by 1895 over the decaying Chinese feudal army resulted. (This is not surprising when it is borne in mind that the 5 million silver tael intended for modernising the Chinese army had been spent by the Empress in building a beautiful marble summer palace near Beijing). Japan exacted a very large sum from China as indemnity, and insisted that this should be paid in sterling and not taels. This broke the back of the Chinese economy since the sum was much larger than Chinese foreign exchange reserves and entailed borrowing.

Japan also acquired the Pescadores group of islands, and the large island of Formosa (Taiwan) from China as colonies, besides a strong economic influence in Korea. Formosa was valuable in providing a semi-tropical climate for growing sugarcane, which was grown with difficulty in Japan only in her southernmost regions. Formosa was rapidly developed as a supplier of sugar and rice to Japan; similarly Korea became increasingly important as a source of rice imports into Japan to supplement inadequate domestic production. After formal annexation to Japan in 1910, Korea's northern regions were also intensively exploited for their mineral wealth.

In both Taiwan and Korea (after 1910), the local population was heavily taxed. Most of the taxation proceeds was remitted to Japan in the form of an export surplus of commodities (rice, sugar, minerals) against which the colonised producers had no claim to yen incomes. This is the typical process of one-way transfer from the colony to the metropolis in the form of an export surplus on merchandise account, not matched by any payment from Japan to her colonies. This kind of colonial transfer characterised the India-Britain relation over an even longer period giving rise to what Dadabhai Naoraji termed the Drain of Wealth from India to Britain. For accounting purposes in the balance of payments, to offset the export surplus which the colonies had, various invisibles charges were imposed by Japan on them. Those were by way of service charges of Japanese personnel, freight and financial commissions, and interest on Japanese investment. In short the colonies were made to pay the costs of their own subjugation and administration.

The Russo-Japanese War of 1904-05, and the First World War, led to further territorial gains and enlargement of her sphere of influence for Japan. Victory against Tsarist Russia in 1905 brought Japan unchallenged control over Korea, the southern part of Sakhalin, control over Ku Liaotung Peninsula and Southern Manchuria. In the first World War Japan gained greatly from the 1918 Versailles Treaty by siding with Britain against Germany during the War, and signing secret pacts with four European imperialist countries (France, Britain, Russia and Italy). As a consequence Japan got control over the German interests in China particularly in Shantung, which Japan had already occupied by 1914. Japan also got ratification for its 'Twenty-one Demands' which it had imposed on the Chinese government in 1915.

The Demands were divided into five groups:

- a) Exclusive and expanded privileges in Shantung;
- b) The Manchurian leases to be extended to 91 years plus right of land ownership.
- c) Rights to mining and railway enterprises in S. Manchuria and eastern Inner Mongolia.
- d) Joint ownership of the Hanyehping Iron Co. on the Yangtse river plus exclusive rights to iron deposits near Hangknow; a ban on China ceding any harbour or island along its coast to imperialist countries other than Japan.
- e) Joint administration of the police force in China; further railway rights and other exclusive rights; and a pledge that, China would buy at least half its munitions from Japan.

The Chinese government agreed to most of the demands in a treaty signed in May 1915, except only group e, and Japan acquired an absolutely dominant position on the Chinese mainland.

7.3.2 Progress of the Basic and Producer Goods Industries upto 1913

Before the establishment of the Yawata Iron works in 1901 as a state owned and operated concern, the domestic output of pig iron and steel was very small. Only 26,000 tons of pig iron was produced meeting two fifths of total home consumption, the bulk, or three-fifths, being imported. The domestic consumption of steel was 222,000 tons, of which 99 per cent was imported. Although some more private concerns were established, by 1913 Japan was still substantially dependent on imports.

Table 7.3
Per cent of Domestic Production to Consumption

		Pig Iron	Steel	Iron Ores
	1896	40	2	—
	1913	48	34	27
Output M. Tons	1913	0.243	0.225	

Source: Allen, Short Economic History of Japan, p.80

The main problem with the iron and steel industry in Japan was the supply of ores. Domestic sources provided only just over a quarter of the requirement of the domestic industry even though this was so small. Nearly 75 per cent of iron ores came from Korea and China. Coal-mining however was more successful and output grew 30-fold from 1880 to 1914.

Table 7.4
Annual Average Coal Output (1877-1914)
Total Output (million metric tons)

Period	Annual Average
1877-84	0.8
1885-94	2.6
1895-1904	8.0
1905-14	16.8
1914	22.0

Source: Allen (ibid). p. 81.

Japan had abundant water-power for electricity generation. This potential began to be tapped seriously after 1900 when marked increase in the use of electricity for lighting, street traction and factory machinery was taking place.

Table 7.5
Electricity Generation: Hydel and Thermal

	Electricity Generation (million Kwh)	Per cent by source	
		hydel	thermal
1907	0.115	33.3	66.6
1914	0.716	55.6	44.4

Source: Allen (ibid.) p. 84.

All branches of the electrical engineering and appliances industries also expanded rapidly. This is one sphere in which foreign capital showed interest. The General Electric Co. of the USA acquired, in 1905, interests in the Tokyo Electric Co. and reorganised it. It also acquired control over the Osaka Electric Lamp Co. a year later. A number of Japanese Zaibatsu also set up electrical engineering works. Thus (1) Mitsubishi Co. set up a department for making electrical equipment for ships and mines, (2) the copper-mining interest of the Kuhara group was diversified to set up the Hidachi works, which became one of the largest engineering firms. (3) Mitsui was associated with the Shibaura Works, while (4) two of the big zaibatsu in the copper trade (Furukawa and Sumitomo) controlled the chief electric wire and cable works. (5) Mitsubishi and Kawasaki had large mechanical and electrical engineering works associated with their shipyards.

Table 7.6
Paid-up Capital: Engineering and Electrical Industry

	General Engineering Industry		Electrical Supply Industry
1895	2.6	1893	2
1903	14.6	1907	12
1913	61.1	1913	200

(million yen)

Source: Allen p. 84.

As regards shipbuilding capacity, this was promoted by the Shipbuilding Encouragement Act of 1896 and an amendment to the Navigation Subsidy Law in 1899. The first provided for a subsidy of 12 yen per ton and 20 yen per ton for ships below and above 1,000 tons respectively; 5 yen per Horse-power was given to marine engines manufactured in Japan. The second measure provided that owners of Japanese built ships could claim twice the amount of subsidy to which Japanese operators of foreign ships were entitled. As a result, the annual average tonnage of ships built rose over five-fold—from below 10,000 tons in the nineties to over 50,000 tons by 1909-13.

Among other large scale industries set up in the pre-first War period, were cement, glass, paper, chemical fertiliser, sugar refining and beer brewing. All these were undertaken by the zaibatsu houses, often with state help. For stimulating sugarcane production in Formosa, from 1902 the state imposed high tariffs on cheaper hitherto imported Javanese sugar and gave large subsidies in addition to Formosan companies. Cane production trebled during the next decade and provided an increasing share of the raw material for sugar refining industry which had originated with refining Japanese raw sugar. A system of duty drawbacks encouraged the industry to export refined sugar after meeting the domestic sugar demand by refining Formosan sugar. This process of State-aided import substitution and export promotion contrasts with the situation in India. The original home of the sugar cane, an unprotected India had become, by the third quarter of the 19th century, a net importer of Javanese sugar and this situation continued until the 1930s.

7.3.3 Consumer Goods Industries and Foreign Trade

The most important light industries were the textiles—silk, cotton and wool. The main role of government in silk and cotton textiles was to import modern capital equipment and set up model spinning and weaving factories which private entrepreneurs could imitate. Woollen textiles, however, comprised an entirely new industry and the Government mill remained the most important plant until the turn of the century.

a) Cotton Textiles

The opening of Japan to Western trade had the immediate effect of a flooding of the Japanese market with cheap machine-made yarn which displaced domestic handicraft spinners (just as had been the case in India half a century earlier). Imports of cotton yarn rose nearly 14-fold, from 12 thousand to 158 thousand bales between 1868 and 1888; the proportion of yarn imports to total imports ranged between 22 and 41 per cent during 1868-1878.

The first modern spinning mills, set up in 1867 and 1872, were not commercially successful owing mainly to their small scale. The industry made little headway for some time despite state encouragement by way of setting up model factories, imports of modern spinning machinery and sale on easy instalment plan to capitalists, and by providing cheap credit. The first large-scale mill, with 10,000 spindles driven by steam-power, set up in 1882, was, however, a financial success. The main spurt of expansion came towards the end of the century when in 1896 a tariff on cheap Indian raw cotton was removed. A rapid rate of inflation lowered real wages of labour, and the acquisition of control over Taiwan and Korea opened up new colonial markets for yarn. The plague in Bombay led to the Chinese government imposing a ban on imports of yarn from there and Japan also seized this opportunity of getting a

Table 7.7
Growth of the Cotton Spinning Industry

	No. of Spindles (000)	Output of Yarn (m. lb.)	No. of Spinning Cos.	Spindles per Enterprise
1887	77	—	—	—
1893	382	88	40	95.5
1897	971	220	74	—
1903	1381	317	51	—
1907	1540	393	42	—
1913	2415	607	44	—

Source: Allen, p. 72.

The industry was built, after 1890, almost entirely on the basis of imported raw cotton, China being superseded by British India as the chief source of supply and the USA also becoming important.

In cotton weaving the displacement of handloom production was much slower as the traditional Kimono cloth continued to be produced on home looms and in 1890 there were over 7 lakh handloom compared to 0.32 lakh power looms. The spinning mills, then around 1903, started setting up power-looms using their own yarn output, to produce standardised wide piece goods (shirtings, sheetings and drills) most of which was exported to Korea, Manchuria and China. The domestic market was shared between a rapidly growing powerloom sector and a continuing large handloom sector. Many early factories installed powerlooms and handlooms side by side. The average size of weaving sheds was quite small with around 40 workers and only about half the 2087 enterprises had power-driven machinery. Some 5 lakh workers still operated handlooms in their homes.

b) Silk Textile Industry

As earlier mentioned, this traditional industry received an unexpected boost in the 1870s from the outbreak of silk worm disease in Europe, and the depreciation of silver, which cheapened exports to gold standard countries. As a consequence raw silk production expanded rapidly and exports comprised as high as 60 to 80 per cent of production.

Table 7.8
Production and Export of Raw Silk (000 Kwan)

	Output	Export	Percent of Output
1868	278	175	62.9
1883	457	365	79.8
1889-93	1110	662	59.6
1899-1903	1924	1110	57.7
1909-13	3375	2563	75.9

Source: Allen, p. 67.

Upto 1880 there was a flourishing export of silkworm eggs, after which the peasants engaged in this turned to cocoon production. Foreign demand for Japanese silk continued to grow and, by 1893, there were 3203 silk reeling factories of above 10 workers, and, of these, four-fifths had machine reeling. However, during 1889-93, more than half the silk output continued to come from household and very small enterprises with less than 10 workers. It was only during 1893-1913 that the filatures surged ahead of hand reeling and, by 1909-13 were producing 72 per cent of the total output.

The government licensed the egg-raisers; and the Yokohama Specie Bank, along with the great export houses, financed the industry by providing loans, through the *tonya* or commission agents, to the thousands of small producers who needed working capital for purchasing cocoons from the farmers. The large filature firms had their plants scattered in rural areas and maintained close touch with the egg and cocoon producers. In this way, even though the raw silk industry was rurally dispersed, financial control was exercised, and the quality control and standardisation necessary

In the pre-first war period unlike silk **reeling** the silk **weaving** industry was little affected by modernisation. The famous specialist weavers of Nishijin continued their highly organised traditional production. However, peasant households continued to weave silk on handlooms, (each region with its own speciality) often under a putting out system where the local merchants provided the weavers with the raw material. The main sphere in which use of power-looms developed was in the production of silk fabrics for export to the USA; but even here, by 1913, only two-fifths of the looms were power driven.

c) Woollens and Worsted

As an entirely new industry which started in 1877, this branch of textile production was organised on a factory basis from the beginning. The demand arose for uniform cloth for the armed forces, blankets and flannels. The setting up of a government factory in 1877 for making army cloth with German machinery and technicians, was followed by a number of private firms. The heavy woollen branch however grew only by fits and starts depending on military demand. Steady and rapid growth was registered however in the production of **muslin** (used for kimono as a substitute for cotton and silk) which used wool as a raw material.

Table 7.9
Output and Imports of Woollens and Worsted

	Out Pur		Imports		
	Muslin m.yd.	Seage m.yd.	Woollens m.yd.	Raw Wool m.lb.	Woollen Yarn m.lb.
1899-1903	8.83	0.28	0.82	6.63	1.14
1904-08	19.61	0.49	2.67	11.74	3.68
1909-13	51.12	3.78	1.54	10.10	5.66
1913	69.58	9.65	1.76	11.16	9.38

Apart from textiles the other consumer goods industries which developed during this period was the manufacture of bicycles.

The Meiji era ended in 1912. In Section 7.4 we discuss the economic developments that took place during Taish era (1912-26).

Check Your Progress 2

1. What are the economic reasons that prompted Japan to colonise her neighbouring territories?

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

2. What was the role of the Zaibatus in the development of new industries?

.....

.....

.....

.....

.....

-
-
-
-
-
-
3. Name five zaibatsus of Japan and five large scale industries that were set up in the pre-first War period in Japan.

-
-
-
-
4. What were the reasons that led to a rapid increase in the production of Cotton textiles in Japan in the 1890s?

7.4 BOOM CONDITIONS IN WORLD WAR I

It has been observed that periods of war and crisis in the advanced capitalist countries have been periods in which the developing countries have made some progress industrially, or have succeeded in partially freeing themselves from old patterns of domination. This is not surprising, for typically during periods of war or economic crisis, the advanced countries have to divert a substantial part of their domestic resources and shipping services to unproductive uses. This, therefore, provides a temporary economic space which can be occupied by enterprising less developed nations, while the political situation is one of flux as well for the developed countries.

The first World War which engulfed Europe, provide such an opportunity for Japan. Before the War, despite the beginnings of modern large scale industry, the overwhelming bulk of manufacturing workers in Japan were still, as we have seen, either household workers or in very small enterprises. However, with the rapid growth of industry under war time boom conditions however, the economic landscape in Japan began to alter decisively.

7.4.1 Effects of the War on Industry and Trade

The belligerent nations in Europe soon faced a shortage of shipping; both of warships and of merchant ships. This affected their trade with Asia, while war also generated a high demand for munitions. Given her history during 1868-1913 in building up precisely these sectors, Japan was well-placed to step up shipping tonnage and munitions production. At the same time Japan also moved quickly to fill the partial vacuum created by war time decline of supply of exports, mainly textiles and machinery, from the west to the colonised and underdeveloped countries in Asia.

The Allied governments started placing contracts for munitions with Japanese firms, and there was a strong and rising demand for the services of Japanese shipping. At the same time Asian markets were wide open to Japanese exporters because of the failure of Britain, Holland and France to keep their colonies' current demands supplied. This period of war boom, which lasted until early 1920, saw not only a substantial enlargement of existing industries but also the setting up of new industries.

Table 7.10
Growth of Selected Industries—1913/14 to 1920

Period year	Steamships tonnage (m.)	Net Income from freight (m.yen)	Coal (m.ton.)	Finished steel (000 ton)	Cement (000 ton)
1913/1914	1.5	40	21.3	255	645
1920	3.0	450	29.2	533	1353

Year	Electric Power (m.kw)	Chemical Fertiliser (m.ton)	Cotton Yarn (m.lb.)	Raw Silk (m.kwan)	Employment in Factories with more than 5 workers (m)
1913	597	n.a.	607.2	3,741	0.948
1920	1378	0.589	726.8	5,834	1.612

As a consequence of the ten-fold rise in revenue from shipping, from exports of munitions and other manufactures, combined with restriction of supply of imports from the West, between 1914 and 1919, Japan built up a large trade surplus and huge foreign exchange reserves totalling over 3000 million yen. Japan's net foreign indebtedness at that time was 1300 million yen. Rather than repay her foreign debt, the foreign exchange was applied to purchasing gold for strengthening the gold reserves of the Bank of Japan and of the Government.

Table 7.11
Gold Reserves of the Bank of Japan and the Japanese Government (m.yen)

Date	in Japan	in N.York	Total	Note issue m.yen
Dec. 1914	129	213	342	385
Dec. 1920	1116	1062	2178	1555

It was owing to a ban on gold movements from the USA. that Japan's foreign holdings of gold rose so substantially. Along with the domestic reserves the foreign holdings too counted for purposes of note issue. With the rise in reserves there was a large increase in the note issue and a trebling of prices of commodities occurred. The rate of inflation in prices of foodgrains and other necessities was higher than the average. This caused acute economic distress to all wage earners and those dependent on purchasing food with relatively fixed salaries.

7.4.2 Price Inflation and the Rice Riots

It is a general feature of periods of war boom that a profit—inflation occurs. In short, the prices of basic wage goods rise faster than all other prices. This leads to a fall in real wage, since money wages do not keeppace with inflation. Conversely, the capitalists in the expanding industries and the traders enjoy a profit bonanza. Since labour organisation in Japan was at a rudimentary stage, a very large fall in real wages took place — by as much as 40 per cent between 1914 and 1918. The number of workers affected was nearly twice as large as before the War.

Table 7.12
Index of Real Wages

Year	(1914=100)
1914	100
1916	74
1918	61

Source: Halliday (1975).

For the poorest industrial workers the prospect was of starvation. The agricultural labourers and poorer tenants were also badly affected. Acute social tensions erupted in the two months long 'Rice Riots' which started in July 1918. With rice prices soaring, a group of women at the port of Uotsu, refused to load ships with grain for export. On August 10 there was a major revolt in Kyoto and the army was called out

extreme violence. After this the uprising became generalised and embraced wider demands.

The peasants revolted against their landlords with land tenure and share cropping contracts as the key issues. Slum-dwellers attacked the offices of a property company which had raised slum rents, and the outcaste **burakumin** were particularly active in the revolts. A strike by the miners of Ube (Yamaguchi prefecture), which led to 13 miners being shot by the Army, sparked off a series of mine strikes lasting until mid-October of 1918.

In all, it is estimated that 10 million people, or nearly one-fifth of the total population of Japan, took active part in the revolts. Uprisings took place at 636 places—mainly in the rice producing areas in western Japan; and there were 107 interventions by the Army. Eventually, the military and police suppressed the uprisings, made over 8,000 arrests, of whom over 500 people were indicted with varying terms of imprisonment.

The Rice Riots of 1918 revealed a basic weakness of the industrialisation strategy in Japan, arising from the highly authoritarian nature of the social and political structure. This in turn was based on the high degree of concentration of productive and financial assets in a hands of a few industrial houses, which was actively promoted by government policies. In consequence the interests of the ordinary Japanese who kept the wheels of industry turning and worked hard in the mine and fields were neglected in favour of the interests of the landlords and the **zaibatsu**. Government hardly ever intervened to stabilise the livelihood of ordinary people. Rather it allowed them to face the brunt of rapid inflation and deflation.

This had certain economic consequences which in the long run were detrimental to the economy. Firstly, it meant that the share of labour incomes in national income in Japan was much lower than in other capitalist countries (about 42 per cent in the thirties compared to around 55 per cent in **Britain** and 60 per cent USA); and moreover this share tended to decline over time. As a result the internal or domestic market for manufactured goods did not expand fast enough. This in turn led the **zaibatsu** to seek external markets and to actively acquiesce in militarisation and the colonial domination of other Asian countries.

Secondly, the high levels of rents which tenant farmers had to pay to landlords impoverished them and restricted the rate of investment in agriculture. This resulted in a marked slowdown in the growth rate of rice and other crops in the post First War period, from a pre-War rate which itself was unimpressive compared to early overestimates. After the Rice Riots of 1918 strikingly exposed the weakness of Japan's food economy, the government accelerated the development of foodgrains production in the colonies, and the transfer of wage goods from the colonies via export surplus to Japan (see Unit 6)

The industrial structure of Japan changed decisively during the war with heavy industry's share growing more rapidly than that of light industry:

Table 7.13
Per cent of Income Originating in Industry

	Heavy Industry	Light Industry	All Industry
1895	19.1	80.9	100.0
1920	38.0	62.0	100.0

The concentration of personal incomes increased markedly, with the share of the top decile of income earners going up to as high as 44.6 per cent by 1919:

Table 7.14
Share of Top 10 per cent in National Income

1895	37.1
1900	35.0
1912	37.7
1919	44.6

industrialisation and the growing role of the colonies. Vis-a-vis the advanced western economies Japan continued to have a typically under developed country's trade pattern exporting mainly agricultural products and semi-manufactures like raw silk while importing mainly manufactured capital goods. Vis-a-vis her own colonies, however, Japan developed the opposite trade pattern, using the colonies as captive markets for her textiles and other manufactures while importing primary sector products and minerals. These trends were reflected in a fall in the share of primary sector exports to total exports, from 48.5 per cent to 13.4 per cent during 1868-72 to 1918-22; and a sharp rise in the share of raw materials plus food imports from 33.1 per cent to 62.1 per cent over the same period.

The war and post-war boom collapsed in 1920. The details of the collapse and measures for recovery, and the onset of agricultural depression, are discussed in the next unit.

Check Your Progress 3

1. How did the First World War benefit the Japanese economy?

.....

.....

.....

.....

.....

.....

2. Was the industrialisation strategy practised in Japan without any weakness?

.....

.....

.....

.....

7.5 LET US SUM UP

In the unit you have read that Japan pioneered the idea of active state intervention at a time when the dominant ideas were of laissez-faire, and free trade. Pre-Meiji Japan had a very narrow industrial base, and a weak infrastructure. The Meiji Japan started operating mines, laid the foundations of a mercantile marine, provided incentive to the Japanese shipbuilders and modernised internal transport and communication. The railways were nationalised in 1906. There was hardly any industrial sector where the government did not invest and use modern technology, be it woollens or cement or chemicals. Once these were operational, under the Transfer law of 1880, many state enterprises were transferred, on favourable terms, to the private sector.

The Banking sector, under the auspices of the government, played an extremely important role by providing credit and initial capital to the private entrepreneurs thereby contributing to industrial development. The banking sector played the role of an intermediary by which savings mobilised from households were lent to the capitalists including the industrial houses (zaibatsus).

Since nature did not favour Japan with a bountiful natural resource base, Japan set to colonise her neighbouring countries which were to provide resources—minerals and foodgrains—at a low cost, for Japan's industrialisation. Also these colonies were converted into ready markets for Japan's manufactured goods. Korea, Taiwan and Manchuria being colonies, Japan could maintain an import surplus with them and benefit from the drain of wealth from these colonies. The Russo-Japanese war of 1904-5 and the First World War led to further territorial gains and Japan's sphere of

Between 1900 and 1913, Japan's industrial production increased rapidly. 75 per cent of Japan's requirement of iron ore was imported from Korea and China. Japan benefited from cheap hydro electricity. Electrical engineering and appliance industries increased rapidly. Cement, glass, paper, chemical fertilisers, sugar refining and beer brewing were the prominent large scale industries set up before 1914. The most important light industries were the textiles—silk, cotton and woollens. Here also the government played an important role by importing modern capital goods and setting up factories which served as model for the private sector. Japanese textiles replaced India's exports to China especially after the plague in Bombay.

During World War I, developed market economies concentrated their resources on production for defence and war, creating a vacuum in international trade. Developing countries, like Japan, worked overtime to fill this vacuum and benefited from an economic boom—especially in shipping and defence related industrial production. Boom conditions lasted till early 1920 when many new industries were set up. During a boom, prices rise faster than the wage rate, thereby increasing the share of profit in an increasing level of output. The fall in real wages of certain sections of workers was rather acute resulting in Rice Riots in July-August, 1918. The peasants also revolted against their landlords demanding land reforms. Miners and industrial workers were also on strike. The Rice Riots exposed a highly authoritarian social and political structure. The share of labour income in the national income of Japan was very low and declining over time. The peasants also had to pay a very high level of rent thereby diminishing the incentive to increase agricultural production.

This period also witnessed a changing industrial production structure. The commodity composition in international trade also underwent a change. The pattern and composition of trade of Japan with advanced capitalist countries was markedly different from that of its colonies—the latter reflecting a typical colonial pattern of trade.

7.6 KEY WORDS

Leading Sector: Certain sectors take the 'lead' in Industrial Revolution—cotton textiles for U.K. and large scale capital goods industries for USSR. Those sectors provide inputs for other industries to flourish (as in USSR) or generate resources for further investment in other productive channels.

Prefectural Bank: Rural banks.

Tael: Silver.

Zaibatsu: Japanese industrial houses e.g. Mitsubishi, Kawasaki, Mitsui, etc.

7.7 SOME USEFUL BOOKS

Refer to Unit 8 for the names of the books.

7.8 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) Read Sections 7.2.1 and 7.2.2 and answer
- 2) Read Section 7.2.3 and answer

Check Your Progress 2

- 1) Read Section 7.3.1 and answer
- 2) Read Section 7.3.2 and answer
- 3) Read Section 7.3.2 and answer
- 4) Read Section 7.3.3 and answer

Check Your Progress 3

- 1) Read Section 7.4.1 and answer

UNIT 8 JAPANESE INDUSTRIALISATION IN THE INTER-WAR PERIOD

Structure

- 8.0 Objectives
- 8.1 Introduction
- 8.2 Aftermath of the Post-war Boom
 - 8.2.1 The Collapse of the Boom
 - 8.2.2 Taisho Democracy
 - 8.2.3 Effects of the Tokyo Earthquake
- 8.3 World Depression and its Impact on Japan
 - 8.3.1 The Decline in Agricultural Prices and Effects on the Peasantry
 - 8.3.2 Redirection in Foreign Trade : the Seizure of Manchuria
 - 8.3.3 The Industrialisation of Manchukuo and Korea
 - 8.3.4 Financing of Reflation, 1931-37
- 8.4 The Second War and its Economic and Social Effects
- 8.5 Let us Sum Up
- 8.6 Key Words
- 8.7 Some Useful Books
- 8.8 Answers/ Hints to Check Your Progress Exercises.

8.0 OBJECTIVES

After going through this unit you should be able to:

- specify the features of Japan's economic and political response to the crisis of the Great Depression;
- group the linkage between economic programme of recovery, militarisation and embroilment in war; and
- assess the effects of defeat on Japan in the Second World War.

8.1 INTRODUCTION

The period between the two world wars must count as one of the most interesting as well as, perhaps, one of the most tragic periods of Japan's economic and social history. At the beginning of the period, up to the mid-twenties, Japan was a newly industrialising nation with a strong and wide industrial base and a strong foreign trade position, beginning to relax tough political controls over its working population in favour of some democratisation. In the course of the thirties, however, a sharp swing to wards the domination of military and aggressively expansionist interests brought the political system to the highest level of repressive fascism. The Japanese people were plunged into war, first against China and then against the Allied Powers during World War II.

The Japanese people suffered heavily because of these military involvements. The production structure gave priority to military needs and civilian consumption within the country suffered. The population of Japan's colonies was subjected to even more intense exploitation than before.

A careful study of the conditions which gave rise to this particular course of military-spending-oriented industrialisation is instructive. It illuminates the strengths as well as the grave weaknesses of the Japanese industrialisation strategy and holds out important lessons for today's underdeveloped countries.

8.2 AFTERMATH OF THE POST-WAR BOOM

The boom in production and trade which marked the period of the First War carried through to early 1920. Every boom must come to an end, however, and in Japan the collapse of the boom occurred from March 1920 onwards. In all other capitalist countries too the war boom collapsed at about the same time.

8.2.1 The Collapse of the Boom

The index of wholesale prices with base 1913, stood at 322 in March 1920, and had declined to only 190 by April 1921. The collapse was particularly severe in rice and raw silk prices. In an attempt to stem the rapidity of the decline the government passed a Rice Control Act and a Silk Valorisation Scheme was introduced. The deflation was not carried as far in Japan as in other capitalist countries, because the zaibatsu, who controlled banking, did not exercise a too severe reduction of the easy credit to industry extended during the war. Such a freezing of credit would have meant many more bankruptcies of enterprises than in fact occurred.

Table 8.1 : Index of Wholesale Prices in Japan, U.K. and the U.S.A.
(Base 1913 = 100)

Date	Japan	U.K.	U.S.A.
Mar 1920	322	307	227
Apr 1921	190	199	142
Dec 1921	209	157	133
Dec 1922	183	152	144
Aug 1923	190	147	140

Source: Allen: *Short Economic History of Modern Japan*, p. 101.

By the end of 1923 Japanese prices were clearly out of line with world prices owing to the smaller degree of deflation in Japan. This resulted in reduced international competitiveness for Japan. An import surplus on merchandise account appeared, totalling Y 824 mn during 1919-22, and invisible earnings from shipping, which had become so large during the war, also declined. The foreign exchange reserves accumulated came in useful and helped to meet the swelling import bills, maintaining exchange value of the yen against the dollar.

8.2.2 Taisho Democracy

The Meiji era ended in 1912 and the reign of the next Emperor, for the brief period 1912 to 1926, is known as the **Taisho**; This was to be followed by the very long reign of Emperor Hirohito from 1926 to 1990, known as the **Showa** era.

The Taisho period saw a growth of labour organisation in Japan, especially after the 1917 Revolution in Russia, which had a strong impact in stimulating labour organisations in many countries. Even though trade unions were not formally banned, the harsh Public Peace Police Law of 1900 in Japan prevented unionisation before WWI. This too gave government the power to intervene against any action or coming together of workers under such vague provisions as 'instigation' or 'temptation' of some workers by others.

The predominance of unmarried young women in the textile sector also made unionisation difficult as these women from rural areas were under the paternalistic control of their employers and indeed even lived in dormitories on factory premises. Nevertheless, between 1906 and 1911, there were a series of strikes by miners and workers in military arsenals which the government suppressed ruthlessly, sentencing the socialist leaders to death and executing most of them.

After the first world war, however, the size of the organised male work force was somewhat larger than before owing to war-time industrial growth. The work-force was radicalised by real wage decline. The Rice Riots, and a series of strike actions were undertaken in the Yawata Iron and Steel Works and the Mitsubishi and Kawasaki dockyards for better wages and work conditions. A Factory Act had been passed in 1911 but not implemented and there was no provision in it for minimum

In 1925 under the mis named Universal Suffrage Law, the right to vote was extended to all males. Women were explicitly excluded as were all those 'who received public or private relief or help for a living on account of poverty'. The number of those eligible to vote was raised thereby from about 3 million to 12.5 million. At the same time in 1925, the government passed a new Peace Preservation Law which was highly repressive. (We may recall that a century earlier in Britain, similarly reform of parliamentary representation under the Reform Bill of 1832 had been accompanied by the harsh New Poor Law of 1834).

Because of the relatively greater activity of workers and of political parties and the extension of the suffrage, the period upto the mid-20s is often referred to as 'Taisho democracy'. However, the very limited nature of democracy during this brief interlude must be borne in mind. Unionised workers never exceeded 5 to 7 per cent of the organised labour force and the main legal union (the *Sodomei*) was thoroughly cowed by repression and indeed gave up strike action. Over half the population (all women and the poor) were debarred from voting representatives to the *Diet*.

The two main political parties were the *Seiyukai*, associated with the *zaibatsu* house of *Mitsui*, and *Minseito*, supported by *Mitsubishi*. Their policies differed little and they represented different cliques within bureaucracy and business. The Japanese Communist Party could only function with great difficulty underground, that is illegally. (Despite their small numbers, however, the adherents of Marxism in Japan whether within a formal political party or outside, had a very strong intellectual impact on the Universities. Monumental research on the nature of the Meiji Restoration and Japanese capitalism, was carried out by the Marxist scholars).

8.2.3 Effects of the Tokyo Earthquake

In 1923 the Tokyo-Yokohama area was hit by a huge earthquake, one of the most lethal recorded in human history. About 100,000 people lost their lives, and virtually the entire Tokyo-Yokohama area was flattened, and large areas burnt in the great fires which raged after the earthquake.

In order to help speedy reconstruction the government adopted an easy credit policy. The Bank of Japan was authorised to discount special bills issued by government (the 'Earthquake Bills') in order to relieve financial institutions whose loans had become frozen owing to the earthquake. The government guaranteed against loss upto 100 mn. yen. The Industrial Bank of Japan and the Hypothec Bank were instructed to make loans on easy terms. A 'reconstruction boom' followed these measures.

Government financed its increased expenditure (owing to the earthquake) mainly by borrowing both internally and on foreign capital markets. With the reconstruction boom the index of wholesale prices recovered to 214 by the end of 1924. But subsequently, a rise in the exchange rate owing to speculation in the yen, disorganised exports and prices again fell steadily. A financial crisis developed since the banks were still substantially burdened by bad loans, and as many as 36 banks had to close their doors. These included the Bank of Taiwan as well as the First Bank, one of the largest ordinary banks. In the crisis of 1927 the delayed post-war readjustment through bankruptcies of a number of enterprises and banks, which had overextended themselves during the war boom, finally took place.

The great Tokyo earthquake was marked by bizarre political events which exposed the underlying deep tensions and conflicts within Japanese society. A pogrom (systematic killing) of many thousands of Korean immigrants, of *burakumin* and of Chinese residents took place. This was done by organisations of the extreme right, with a deeply chauvinistic attitude to foreigners and hatred towards Japan's own ethnic disadvantaged population, the *burakumin*.

The ground for the rise of these organisations had been prepared by the Meiji State itself. At the primary school level, the values of unquestioning obedience to authority in the person of the Emperor, were systematically taught. An admiration for martial values was developed by making six hours of military drill compulsory at the normal school level. Emperor-worship and chauvinism which extolled Japan's military domination over others, had struck deep roots within the population. The secret societies of political activists of the right adhered to these views in an even more

therefore, massacred by these organisations or by the gendarmerie, taking advantage of the chaos unleashed by the Tokyo earthquake. The police murdered nine prominent Japanese labour leaders, including Osugi Sakae and his family, who were killed at Military Police Headquarters.

The absence of the rule of law and of elementary liberal values within the populace at large, reflected the entire character of the development of capitalism in Japan. It occurred, not 'from below' as a democratic process, but 'from above'. It was promoted by an oligarchy which used not only the State but also the educational system to fashion a set of ideas and beliefs subservient to their aims.

Check Your Progress 1

- 1) Briefly discuss the effects of the Tokyo earthquake on Japanese economy. From these effects, draw inference about the character of Japan's capitalist development.

.....

.....

.....

.....

.....

.....

.....

- 2) Compare the change in the index of wholesale price of Japan with that of U.K. and U.S.A. during March 1920 to August 1923. What was its repercussion on Japan's balance of trade?

.....

.....

.....

.....

.....

.....

.....

8.3 WORLD DEPRESSION AND ITS IMPACT ON JAPAN

The reasons for the World Depression starting in the second half of the twenties and lasting until the early thirties, are still debated by economists. Theories of business cycles and of secular cycles of economic activity have been put forward. There are those, on the other hand, who maintain that no theory of periodicity can be satisfactory; an appreciation of a specific combination of economic and political circumstances is required for understanding the Depression.

Certainly the inter-war Depression was more severe and encompassed more countries than any previous occurrence. The volume of world industrial production and of world trade shrank considerably. In the advanced capitalist countries a minimum of one-seventh of the workforce was unemployed in all the years of the Depression, and in the worst three years upto one-fifth was unemployed. The Depression brought a decisive end to the era of free trade. The capitalist countries turned protectionist to salvage what they could of shrinking employment; and the Gold Standard, based on free trade, was abandoned.

In Japan, given the background of existing political authoritarianism and rudimentary growth of democratic organisations, the Depression had not only an economic impact but also a political impact in delivering the death blow to further

8.3.1 The Decline in Agricultural Prices and Effects on the Peasantry

Primary sector prices started declining worldwide earlier than manufactured goods prices. And international terms of trade deteriorated sharply for countries exporting primary sector products. In Japan the decline was of the order of 40 per cent during 1920 to 1937:

Table 8.2 : International Terms of Trade

Selected year	Index of Export Prices	Index of Import Prices	Index of Terms of Trade
1928	100	100	100
1932	57	65	88
1936	68	98	69
1937	76	126	60

Source : Allen *ibid.*, p. 140.

Within Japan the inter-sectoral terms of trade (the ratio of agricultural prices to manufacture prices) also turned against agricultural products. Those engaged in raw silk production were particularly badly hit and thousands of rural households faced ruin. In the course of the year 1930 alone raw silk prices fell by 50 per cent and silk exports that year were 53 per cent only by value (though 82 per cent by volume) of the previous year. In 1931 the situation worsened with a further fall in silk prices. Since this followed a fall by nearly 40 per cent in a single year 1929-30 of rice prices (from 29 yen per koku to 17 yen) the peasantry were faced with the prospect of ruin.

Table 8.3 : Price of Raw Silk

	Yen Per 100 kin
1923	2150
1929	1420
1930	540
1932	390

Source : Allen, p. 117.

Unfortunately, the economic policies of the Finance Minister J. Inouye, in the Minseito Party cabinet, were ill-advised. Misled by a slight rise in 1929 in U.S. demand for raw silk and increased absorption of Japanese cotton textiles by India, Inouye had no inkling of the seriousness of the approaching depression. He followed a rigid policy of balancing the budget through expenditure cuts and permitting free movement of gold. The onset of world depression led to an intensification of the price fall. This fall in price in any case would have been necessary to maintain the exchange value of the yen under the policies of expenditure cuts. Japan experienced a 35 per cent fall in the wholesale price index in the course of 1931.

Government still persisted in its efforts to carry through deflation. Inouye pressed for lowering military and naval expenditures, which was strongly opposed by the armed forces. With the onset of the Depression in the U.S.A. (Japan's main export outlet in the West) and the consequent collapse of 'American prosperity', the U.S.A. raised tariff barriers against Japanese goods. Inouye's policies were discredited and the Minseito government fell. The Army was a barometer of peasant discontent since soldiers were overwhelmingly drawn from the peasantry. The Army was restive and eager to extend its influence in the face of the crisis.

The crisis was accentuated during 1931 because firstly, speculators were buying dollars in anticipation of a fall in the exchange value of the yen, and gold shipments continued. Secondly, Britain's departure from the gold standard and consequent depreciation of sterling generated renewed British competitiveness in Asian markets (which Japan had been successfully penetrating since the First War).

By the end of 1931 the gold reserves of the Bank of Japan were only 470 mn. yen compared to 1,072 mn. yen two years earlier. In December 1931 after the fall of the government a gold embargo was reimposed and the unwise deflationary policy brought to an end. But the form that subsequent reflationary policies assumed were

8.3.2 Redirection in Foreign Trade : the Seizure of Manchuria

As Japan's trade with the advanced capitalist world declined, she turned increasingly to her colonies. More intensive investment in existing colonies and the seizure of Manchuria began a new period of reflationary expenditures, following Japan's departure from the Gold Standard.

The Japanese army stationed in S. Manchuria, generally referred to as 'The Kwangtung Army', unilaterally staged an incident in Mukden (now Shenyang) to provide an excuse for taking over Manchuria. The Kwangtung Army seized S. Manchuria without reference to the cabinet. It was however, obstructed from occupying the whole of Manchuria until December 1931, when the Minseito government fell. Under the new Cabinet N. Manchuria was occupied and in March 1932 a puppet state called 'Manchukuo' was set up with Pu Yi, the last heir to the Chinese throne, as its nominal head. Japan then began on exploiting the mineral resources of Manchuria systematically and also started encroaching on other areas of N. China.

The new Finance Minister, Takahashi, initiated reflationary policies of increasing government expenditures and cheapening credit, from early 1932. The remarkable feature of these policies is that they anticipate the theorisation of counter-cyclical policies by Keynes in his 'General Theory of Employment, Interest and Money', which was published only in 1936. Moreover, Takahashi's policies also predate by a year, reflationary policies undertaken by President T. Roosevelt acting on Keynes' advice, in the form of the famous 'New Deal' which was implemented in the U.S.A. from 1933 onwards. Thus Japan pioneered Keynesian policies of reflation through increased government investment and other expenditures long before Keynes himself had been generally read and understood in the capitalist world.

It is unfortunate, however, that the form that increased expenditure took, was overwhelmingly military and hence, unproductive in nature. While the Finance Minister concerned himself with the economic aspects of reflation alone, the armed forces seized the opportunity to press their demands, citing the increased requirements on the Chinese mainland. The share of armed forces expenditures in the total budget, which was already high at 31 per cent in 1931-32, rose steadily to as much as 47 per cent by 1936-37.

All industries directly and indirectly connected with the militarisation of the economy — munitions, heavy industry, shipping, vehicles, uniform requirements — showed expansion. Since there was excess capacity in industry and unemployment in the rural sector, which provided plentiful reserves of labour to industry, these expansionary measures could be undertaken between 1931 and 1935 with success. The effects of the Depression on Japan thus lasted for a shorter period than in the Western capitalist countries. The index of industrial production rose from 91 to 136 during 1931 to 1936 (with base 1931-33 = 100).

Table 8.4: Index of Wholesale Prices, Selected Years
(1900 = 100)

1920	343	} Collapse of the post-war boom
1923	264	
1926	237	} Depression and Inouye deflation
1929	220	
1930	181	
1932	161	} Takahashi Reflation
1934	178	
1936	198	

Source: Allen, *Statistical Appendix*.

However, the sectoral impact of the reflation was very uneven, given the extreme military bias in expenditures. Agricultural output continued to decline relatively speaking and the frequency and intensity of landlord tenant disputes were proof of the acute dissatisfaction of the peasantry.

Yet, if we compare Japan's trade performance with that of other countries we find that she fared very much better during this period mainly owing to her colonies, where Japan traded on preferential terms dictated by herself. In effect Japan could

made manufactured goods which replaced colonial handicraft production. At the same time they acquired food and raw materials cheaply, or a portion even, gratis, as the commodity equivalent of tax imposed on the colonies. The share of the colonies in Japan's exports rose from 18 per cent to 25 per cent between 1929 and 1936. The share of colonies in Japan's imports rose less, from 20 to 24 per cent over the same period.

Japan also succeeded in partially compensating for the loss of the raw silk market in the U.S. by substantially increasing her share of the Indian market for cotton textiles at the expense of Britain. Japan had first acquired a foothold in the Indian market during the first War when supplies from U.K. to India had been disrupted. Once a consumer taste for Japanese made textiles had been created, Japan made steady advance in wresting the Indian market from Britain. The yen depreciated when Japan left gold standard in 1931 and this further cheapened textile exports. Further, cheap labour relative to Britain and rising productivity enabled Japan to maintain competitiveness even when the colonial government in India started raising tariff barriers against Japanese textiles.

Table 8.5: Gross Imports of Cotton Goods into India (1910-1939)

	from UK mn. yds.	from Japan mn. yds.	Percent to Total imports UK	Japan
1910-1912	2525	2.3	86.4	0.1
1913-1915	2510	21.3	96.7	0.8
1916-1918	1361	144.3	88.5	7.8
1919-1921	1074	112.0	87.6	9.3
1922-1924	1462	128.7	89.4	9.1
1925-1927	1432	294.7	80.7	16.6
1928-1930	1076	413.3	68.0	26.1
1931-1933	0459	420.0	50.9	46.6
1934-1936	0442	429.0	49.9	48.2
1937-1939	0206	370.7	34.0	60.2

Source: Bagchi 1973, *Private Investment in India*.

Of course, the total size of the Indian market for imports had itself shrunk a lot owing to the rise of the Indian textile industry. So 60 per cent of the total imports which Japan accounted for in the late 1930's was less in terms of yardage than a decade earlier when she had supplied 26 per cent of imported textiles. Nevertheless, the maintenance of the Indian outlet was of help to Japan when exports to the West were falling.

8.3.3 The Industrialisation of Manchukuo and Korea

During 1931 to 1936 Japan invested at a fast pace in the development of Manchukuo and Korea. This is the period referred to as the "quasi-wartime economy", when the requirements of the military and navy dominated economic policy. In 1937 Japan was to launch a full-scale attack on China from her Manchurian base. This was preceded in 1936-37 by important political developments which are discussed below.

Exploitation of Korean Mineral Resources

The northern part of Korea is extremely rich in a varied range of minerals, some of which were of great strategic importance for Japan owing to their use in the aircraft industry, then in its infancy. Japan developed Korea in the 1930s as a source of coal, iron ore, pig iron, gold and silver, and the strategic metals like aluminate and molybdenum.

Table 8.6: Production of Minerals and Manufactures in Korea (1926-1936)

Selected year	Gold kg	Silver kg	Value Gold	(m. yen) Silver	Gold & Silver ores '000 tons
1926	7,159	1,571			
1931	9,031	11,404	9,584	0,207	12,858

	Iron ore m. ton	Pig iron m. ton	Steel m. ton	Coal m. ton
1926	0.352	0.118	—	0.683
1931	0.165	0.148	—	0.936
1936	0.234	0.156	0.097	2.282

Source: EB Schumpeter (Ed) *Industrialisation of Japan and Manchukuo*.

It will be seen that the value of the precious metals — gold and silver — extracted from the Korean mines rose over six times to 62 mn. yen over the five years 1931-36. Coal production nearly doubled. Mining of relatively small quantities of high value ores of aluminite and molybdenite rose and registered a five-fold rise in value over this brief period:

Table 8.7: Value of Aluminite and Molybdenite, m. yen.

1910	6.068
1931	21.742
1936	110.503

Source: as above.

The extractive and manufacturing industries were set up in Korea mainly by the **Shinko-zaibatsu** (or 'New-Zaibatsu') groups such as Nissan, Mori and Naguchi, with active Japanese government help by way of cheap credit.

In Manchukuo the Government established four special companies in 1934 and 1935 in cooperation with the already existing S. Manchuria Railway Company. These special companies were: the Manchukuo Petroleum Co., the Manchukuo Gold Mining Co., the Manchukuo Coal Mining Co. and the Manchukuo Mining Development Co. Apart from the minerals mentioned, Manchukuo also became important as a source of aluminium, magnesium, lead, zinc, shale oil, pig iron and iron ores.

The importance by the Japanese government to stepping up production of minerals in the colonies can be understood in the light of the very poor mineral resource base of Japan proper in everything except coal and copper. In consequence, Japan was heavily dependent on imports, a high proportion from non-Asian countries.

In 1935 and 1936, Japanese domestic production of crude petroleum was less than 10 per cent of supply, with the U.S. as the main import source. Imports in those years accounted for 90 per cent of the lead, 60 to 70 per cent of the zinc, tin and aluminium, 100 per cent of the nickel and as high as 40 per cent of even the copper consumed by Japanese industries. Imports also made up about 88 per cent of iron ores, 50 per cent of scrap iron and 30 per cent of the pig iron utilised by Japan's iron and steel industry.

As a consequence of heavy investment and increased production in Manchukuo destined for Japan, growing import surplus for Japan emerged vis a vis this region from 1933 onwards, reaching nearly a billion yen by 1939. The import surplus for Japan was, of course, an export surplus for Manchukuo — the colonial pattern again.

Table 8.8: Foreign Trade of Manchukuo

	Export Surplus, m. yen
1932	-280.5
1933	67.4
1934	145.1
1935	183.1
1936	89.1
1937	242.1
1938	549.3
1939	957.2

Source: EB Schumpeter (ed.) *Ibid*

The Feb. 26 Incident and Swing to Fascism

No account of economic developments in the inter-war period can be given independently of political developments, for, in this period, more than any other, the two were inextricably linked. Fascism is a complex economic and political phenomenon. And there is controversy over whether political developments in Japan in the thirties can be characterised as resulting in 'fascism'. For those scholars who consider that the **specific features** of German and Italian fascism in the inter-war period are essential features of 'fascism' in general, Japan cannot be called 'fascist'. They point out that there was no single political party which called itself a fascist party in Japan, unlike in Italy or Germany, and no single moment of dominance of such a movement which can be identified in Japan (such as the march on Rome by Mussolini). They consider that Japan which already had an authoritarian political structure gradually slid into a semi-military dictatorship. (This view is advanced for example, by Halliday, 1975).

There are however certain **general** features of fascism as an economic, social and political phenomenon which were clearly common to Germany, Italy and Japan. The fact that Japanese developments differed in detail from the European trajectory of fascist dominance, can be explained in terms of the differing initial conditions in Japan. These common general features are as follows :

- all the economies which slid into fascism in the face of crisis, were late industrialisers, with Japan as the most laggard of the three.
- the characteristic of all the late industrialisers was that they did not have any period of wide-based competitive capitalism (where large numbers of small capitalists compete against one another) and
- therefore lacked deep-rooted institutions of representative parliamentary democracy.

Rather, they were characterised by:

- industrial monopoly from the beginning,
- by a close interpenetration of financial capital and industrial capital and by
- authoritarian political and social structures.

As we have seen in Japan the State actively promoted the **zaibatsu** who started as financial oligarchs and controlled through holding companies a wide range of trading and manufacturing interests. Democratic institutions were very poorly developed, with the franchise (right to vote) being restricted to below 5 per cent of the population of males, and with severe repression of labour organisations.

The world depression meant a period of acute economic crisis for the monopoly capitalists, whose profits diminished. In order to maintain their profits these capitalists set about smashing trade union organisations of labour which sought to protect workers' real wages. As long as this was possible within the framework of parliamentary democracy that framework was retained. Where the framework itself was weak, however, (owing to the undemocratic nature of the transition to industrialism) there was a direct seizure of State power by monopoly capitalists. The instruments of State power were then used to discipline labour, culminating in the destruction of unions and execution of labour leaders; and external expansion was launched upon to acquire markets and materials to offset the effects of Depression. This direct seizure of State power and its use in this manner may be said to constitute the essence of fascism.

In Japan no less than in Germany and Italy, intensified attack on labour organisations and banning of all agitation in the name of patriotism and against a background of aggression against other countries, were present as early as from 1937 onwards (with the attack on China). The missing fascist political party was substituted in effect by the army (which often acted independently of nominally elected cabinets) and the charismatic demagogy of a Hitler or a Mussolini was substituted by the peculiarly Japanese phenomenon (deliberately promoted from the early days of the Meiji State) of Emperor-veneration.

The promotion of extreme chauvinism amongst the people through propagating the

idea of it being right to dominate other nations for the glory of the Emperor and of Japan, was very useful to the Showa State in diverting the anger of the people into external channels at their economic plight. Thus a mass base of support for fascist policies was created amongst the peasantry and other small producers, from whose ranks, in turn, the army men were recruited. These small producers, hit by the Depression, were radicalised in a right-wing direction. They identified the cause of their woes as (1) the big *zaibatsu* houses which financially controlled them on the one hand, and (2) organised labour on the other. The anti-*zaibatsu* sentiments expressed themselves in occasional political assassinations of ministers associated with particular *zaibatsu* houses. Such activities were, however, only a minor nuisance for the *zaibatsu*, who made nominal concessions to criticism by donating money to welfare funds.

The anti-organised labour sentiments of the small producers, however, was of great use to the *zaibatsu*. Fascist organisations of the extreme right grew in strength and numbers at the same time that left-wing trade unions of the socialists were developing in the twenties and thirties. These fascist organisations disrupted workers' meetings, beat up and even killed labour leaders and generally acted as instruments of terror vis-a-vis the working class. Their illegal acts were in the interest of the *zaibatsu* who could not directly use such measures; but, on occasion, members of these fascist organisations could also turn against the *zaibatsu*.

In this respect, again, there is a similarity with Germany and Italy, where the radical fascist rank and file was strongly anti-monopoly while being bitterly anti-labour. (These radical anti-monopoly elements were purged from the fascist parties in Europe once the parties seized power and acted directly in the interest of the business houses; in Japan the radical elements ultimately provided the cannon fodder in the wars which served to enrich the *zaibatsu*).

In February 1936, the army attempted a coup and for three days control over Tokyo hung in the balance. On an appeal from the Emperor the troops returned to their barracks. This incident however marked a decisive shift in the locus of power and initiated a period of preparation for war. The nature of the shift can be understood from the fate of the Finance Minister Takahashi.

By late 1935 unemployed resources in Japan were almost fully employed owing to the reflationary policies of large military and related expenditures. Takahashi believed that a halt should be called to reflation as continuing with it would mean a diversion of resources from civilian uses. The military bitterly opposed any cutback on military appropriations in the budget and indeed demanded an increase. This conflict was a major reason for the attempted coup of February 1936, in the course of which Takahashi was murdered by the military. He was replaced by a pliant Finance Minister fully amenable to military control. February 1936 may be dated as the inception of full-scale fascism in Japan.

8.3.4 Financing of Reflation, 1931-37

While discussing reflation in general we have not yet considered the specific measures through which it was achieved. The increase in Government expenditure was almost entirely credit-financed, that is by borrowing, and this was combined with easy credit conditions. The internal national debt nearly doubled from 4.48 billion yen to 8.52 billion yen between March 1931 and March 1936. The proportion of total expenditure going to the Army and Navy rose from 31 per cent to 47 per cent over the same period. Takahashi refused to raise the amounts spent on relief measures in agriculture. He argued that the general rise in expenditures would diffuse to agriculture and other depressed sectors. As a matter of fact, raw silk prices did not recover and in 1936 were still only a little above half the 1929 level. The only way that increased military expenditures would 'benefit' peasants was, therefore, through their increased recruitment into the armed forces to serve eventually as front line soldiers with grave risk to their lives in the battle field.

As part of the 'cheap money' policy the discount rate of the Bank of Japan was lowered from 6.5 per cent to 3.65 per cent between 1931 and 1933 and in 1932 the interest rate of the Treasury Deposits Bureau was cut from 4.2 per cent to 3 per cent. Money supply (note issues) rose by around 40 per cent over 1931-35, and the exchange value of the yen was allowed to fall by 60 per cent over the year 1931-32.

By the end of 1936 wholesale prices rose to the 1929 level. Over this period, when production and employment were rising substantially, the real wage rate of labour declined steeply and thus real earnings were no higher than they had been in 1929; clearly the effects of deflation did not benefit labour. This however was the average effect of quite divergent patterns of wage-movements; in the heavy industries linked to war-preparation, the real earnings rose while in the consumer goods industries they fell substantially.

Table 8.9: Indices of Wage-rates and Earnings (1926 = 100).

Year	Wage Rates A	Actual Rates B	Retail Prices C	Real Earnings D
1929	98.6	103.9	91	114
1930	91.3	90.7	68	137
1932	88.1	88.1	69	128
1936	80.7	91.8	80	115

Source: Bank of Japan, data quoted in Allen p. 138.

The main reason for the strong downward pressure on wages was continuing rural depression and unemployment which led large numbers of workers, mainly female, earlier occupied in the rural silk industry, to now seek work in urban cotton textile and other consumer industries. However, the index of consumer goods output rose from a 1931-33 base of 100, to only 125 by 1936 compared to a rise to 172 for producer goods industries. Although cotton output and exports were rising, technical changes towards higher labour productivity (lower labour/output ratios) were taking place in cotton textiles, so labour absorption was not high. Hence the consumer goods industries saw strong downward movements in real wage rates. Industrial profits rose substantially and export of capital to Manchukuo, in particular, was quite large during this period.

The policy of creating a 'quasi-war time economy' was followed with even greater vigour after the replacement of Finance Minister Takahashi. Since little underemployed resources remained by this date, continuing large credit-financed expenditure by government now led to a sharp rise in the wholesale prices index and export growth slowed. The government imposed exchange restrictions on traders to ensure that priority was given to imports of strategic war materials. In 1937 the Japanese army in Manchukuo launched war against nationalist China on the pretext of the 'Marco Polo Bridge' incident.

Check Your Progress 2

- 1) Provide a brief commentary on the deflationary economic policies pursued by the Japanese Finance Minister J. Inouye between 1929-31.

.....

.....

.....

.....

.....

.....

.....

.....

- 2) Why were Japan's trade policies better than those of developed countries during the Great Depression?

.....

.....

.....

.....

.....

3) In what ways did the industrialisation of Korea and Manchukuo benefit the Japanese economy?

.....

.....

.....

.....

.....

.....

.....

.....

4) Why did all imperialist countries maintain import surplus with their colonies? How could they afford to do so?

.....

.....

.....

.....

.....

.....

.....

.....

5) Distinguish between the characteristics of the Japanese fascism and German fascism.

.....

.....

.....

.....

.....

.....

.....

.....

6) How was the reflation financed in 1931-37?

.....

.....

.....

.....

.....

.....

.....

.....

8.4 THE SECOND WORLD WAR AND ITS ECONOMIC AND SOCIAL EFFECTS: 1937-45

“From the outbreak of the war with China in July 1937 until the defeat (of Japan) in August 1945, Japan poured all its strength into the war and in so doing was destroyed — ” (T. Nakamura, The Post War Japanese Economy). Since the Japanese economy, particularly the industrial sector, was near full employment of resources by 1936, the inception of war against China saw controls being imposed from the beginning to divert resources from civilian needs to military requirements.

The Army had drawn up a Five Year Plan for key industries based on the ideas of the Chief Operations at the Army General Office. This was intended as preparation for an expected war against the Soviet Union. The war against China broke out somewhat on the lines of the Manchuria Incident six years earlier. It was the local troops who provoked the Marco Polo Bridge Incident, and the assault on China was ratified only later by Tokyo. Having engaged China, however, the Army planned to extend hostilities rapidly. The puppet cabinet (both the Finance Minister and the Governor of the Bank of Japan had been installed by the Army) drew up a total military appropriation of 2.5 billion yen or over 90 per cent of the year's budget of 2.8 billion yen. In 1938 conscription began.

Table 8.10: 1937 Five Year Plan Capacity Expansion Targets (per cent per annum)

	Coal	Oil	Steel	Electric Power	Machine Tools	Aluminium	Magnesium	Ship Building
Japan	1.7	15.5	2.0	1.7	3.5	3.3	12.0	1.7
Manchukuo	2.8	15.6	8.9	3.0	n.a.	n.a.	n.a.	n.a.
Total	2.0	15.6	2.7	1.7	3.8	4.8	18.0	1.9

n.a.: not available

Source: T. Nakamura

In October 1937 the government's newly set up Planning Agency began working on a 'materials mobilisation plan' to allocate foreign exchange to a targeted value of imports. As materials shortages grew the control system was tightened up. Two orders were passed under which broad control was ensured in such areas as the behaviour of firms, their disposal of profits and the financial institutions' use of funds.

Imports fell and as the armed forces were given priority, civilian consumption was squeezed. With the outbreak of war in Europe in 1939, in anticipation of export prohibitions from the countries involved, Japan mobilised whatever foreign currency was available, including drawing down the reserves of the Bank of Japan, to build up stocks of strategic goods like petrol, iron, nickel and cobalt. During 1939, with increasing shortages, full-scale controls were extended over the entire economy. The use of cotton goods to meet private demand was banned and a ration coupon system for steel and other metals was adopted. Market prices soared and a flourishing black market emerged, to counter which an economic police force was created. A ceiling was placed on prices and wages by the 'Stop Order' of September, 1939. At the same time owing to drought in western Japan and Korea, a crisis arose over food supplies and hydel power.

Japan concluded a tripartite alliance with Italy and Germany in 1940. The U.S.A. imposed an embargo on scrap iron and machine tools exports to Japan but continued to supply petroleum. When Germany invaded the Soviet Union in June 1941, Japan quickly expanded into S.E. Asia by occupying southern Vietnam. The U.S.A. then imposed an embargo on the supply of aircraft fuel and other petroleum products and froze Japanese assets in the U.S.

The calculation of the Japanese military was, undoubtedly, that the conquest of Asia would be achieved within two years. For in 1941, Japan's stocks of oil were only 8.4 million Kilolitres, sufficient to keep naval operations going for two years only. As we have seen Japan imported nine-tenths of its oil (there were large unexplored oil reserves in Manchukuo and the Bohai sea, but the Japanese colonisers did not know it then). The Army launched on the conquest of Philippines, Singapore and Indonesia in a series of rapid campaigns.

Within Japan the burden of war financing was borne by the workers via sharp fall in real wages to even lower levels and by the civilian population at large via a drastic fall in consumption. As T. Nakamura puts it, "... the industrial sector was distorted into a swollen military production sector and a subsistence commodities sector that was squeezed to the utmost".

By 1944, Japan was already economically defeated by the oil embargo; further, her shipping losses had been much higher than the initially estimated 0.6 to 0.8 million tons a year and she was unable to compensate by maintaining shipbuilding

below 2 m tons by 1944. The indices of production in the various industries during the war period tell the same story.

Table 8.11: Decline in Production Indices, 1941-1945
(Base 1937 = 100)

	1941	1945
Agriculture and Forestry	95.1	59.3
of which Rice	83.0	59.0
Mining and Manufacturing	123.0	53.1
of which Machinery	188.0	107.2
Steel	132.0	51.8
Food Products	78.1	31.6
Textiles	60.4	6.4

Source: T. Nakamura, Ibid.

With the bombing preceding defeat, Japan lost a high proportion of productive capacity and the major cities like Tokyo and Osaka were virtually flattened to the ground. The USA took advantage of the fact that Japan had not formally surrendered, (even though it was clear that she was economically and militarily defeated) to test its new atomic weapons by dropping them on Nagasaki and Hiroshima, with a tragic destruction of civilian life and genetic effects on the population which persist to this day. The promising beginnings of a modern society with the Meiji Restoration of 1868 thus culminated in the humiliating Showa Defeat of 1945 and the Occupation of Japan by the USA.

Check Your Progress 3

1) What are the economic reasons for Japan's military defeat in the Second World War?

.....

.....

.....

.....

.....

.....

.....

.....

2) How did Japan finance its war time expenditure?

.....

.....

.....

.....

8.5 LET US SUM UP

The Japanese economy enjoyed boom conditions till early 1920, when the boom collapsed severely depressing rice and silk prices and leading to bankruptcies of enterprises. Japan lost her international competitiveness for a time owing to a lower rate of deflation compared to UK and USA. The Tokyo Earthquake of 1923 resulted in a new reconstruction boom. However, in the political sphere, the aftermath of the earthquake was characterised by systematic killing of Japanese untouchables — the burakumin — and the development of rightist, anti-labour tendencies. It showed clearly the peculiar characteristic of Japan's state-promoted capitalist development.

The World Depression of 1930s brought an end to the era of free trade. International trade and industrial output shrank dramatically in the countries of late industrialisation and protectionism reigned supreme. Labour was suppressed and the economy and polity began to be dominated by the rise of fascism. During the depression, the terms of trade moved against the primary commodity exporting countries including Japan. With the drastic decline of silk prices, thousands of households depending on silk production faced ruin, while the fall in rice prices affected all producers. Deflationary policies by the Finance Minister Inouye accentuated depression further. The discontent of the depression-hit small producers was channelised by the rightist organisations.

Prices fell at a faster rate than those of Japan's competitors. But since a protectionist international trade regime was prevailing, Japan's increased competitiveness did not boost her exports. Simultaneously, Britain became more competitive in Asian markets. In December 1931, the government fell and the era of reflationary policy began under Takahashi. While government expenditure increased it was directed basically towards unproductive military expenditure; however, the underutilised labour and production capacity was utilised leading to an increased industrial output. While production and employment rose owing to the reflationary policies of 1931-37, the real earnings of labour in 1937 was no higher than the level prevailing in 1929. This was mainly due to continuing rural depression and unemployment. Manchuria was seized and a puppet state called 'Manchukuo' created by Japan, in 1932.

Japan's dependence on her colonies like Manchuria and Korea increased during this period. Japan's trade with India also increased in the thirties. Japan invested in the exploitation of the mineral resources of Korea and Manchukuo. The colonies were forcibly converted into a lucrative market for Japanese manufactures and became even more important than before, as a cheap source of Japanese imports of agricultural goods, minerals and industrial raw materials. Japan was able to maintain an import surplus with her colonies without balance of payments problems — a characteristic of the colonial pattern of trade. However, with regard to a very crucial import — petroleum — Japan remained dependent on the USA for nine-tenths of her requirements.

From February 1936 onwards, economic policies in Japan increasingly reflected the goals of military expansionism as a part of the triumph of fascist tendencies. In Japan, the parliamentary tradition was not deep rooted and the military had always significantly influenced Japan's economy and polity but now it dictated policy, via puppet Finance Ministers and Governors of the Bank of Japan. The policy of creating a 'quarter war time economy' was followed vigorously. Industrial production and investments were geared to the needs of the military increasingly at the cost of civilian consumption. Japan launched a full-scale assault against China in 1937, and with the outbreak of war in Europe in 1939 allied with fascist Germany and Italy. Japan launched on a series of rapid campaigns in Asia and seized Philippines, S. Vietnam, Singapore, and Indonesia.

Faced with growing shortages, Japan increasingly became a control based economy resulting in a flourishing black market and zooming open market prices. The strategic calculation of the Japanese military that victory would be achieved within two years, did not materialise as the war on the Asian front continued unabated. Industrial production declined drastically during 1943-45. The economic defeat of Japan contributed in a large measure to the humiliating defeat of the Japanese army in the Second World War — an anti climax to the rapid progress made by Japan since the Meiji Restoration of 1868.

8.6 KEY WORDS

Cheap Money Policy : A relationary policy of increased money supply leading to a reduction in interest rate, increase in the level of investment and the level of output.

Diet : Japan's Parliament

Gendarmerie : police force.

Quasi-war time economy: Economic policies giving top priority to the needs of the military even in times of peace resulting in reduction in resource allocation to the civilian sector at times of full employment.

8.7 SOME USEFUL BOOKS

Allen, G.C. 1972. *A Short Economic History of Modern Japan*, Allen and Unwin, London.

Bagchi, A.K. 1972 *Private Investment in India* Cambridge University Press, London.

Halliday, 1975. *A Political History of Japanese Capitalism*, Pantheon Books, New York.

Nakamura, T., *The Post War Japanese Economy*, University of Tokyo Press, Tokyo.

Schumpeter, E.B. (ed.) *The Industrialisation of Japan*.

8.8 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) Read Section 8.2.3 to answer
- 2) Read Section 8.2.1 to answer

Check Your Progress 2

- 1) Read Section 8.3.1 to answer
- 2) Read Section 8.3.2 to answer
- 3) Read Section 8.3.3 to answer
- 4) Read Section 8.3.3 to answer
- 5) Read Section 8.3.3 to answer
- 6) Read Section 8.3.4 to answer

Check Your Progress 3

- 1) Read Section 8.4 to answer
- 2) Read Section 8.4 to answer

UNIT 9 ECONOMIC DEVELOPMENT IN RUSSIA 1860-1917

Structure

- 9.0 Objectives
- 9.1 Introduction
- 9.2 Background
- 9.3 Agriculture
 - 9.3.1 Emancipation Act and Its Consequences
 - 9.3.2 Post 1861 Agricultural Development
 - 9.3.3 Reforms of 1905 and 1910
- 9.4 Industrial Development in Pre-War Period
 - 9.4.1 Emancipation Act and Industrialisation
 - 9.4.2 Overall Economic Development
- 9.5 Let Us Sum Up
- 9.6 Key Words
- 9.7 Some Useful Books
- 9.8 Answers/Hints to Check Your Progress Exercises

9.0 OBJECTIVES

After reading this unit you will have an idea of :

- the problems and contradictions of agricultural and industrial development in the years preceding the October Revolution.
- how these problems were sought to be tackled by the government of Imperial Russia and the policies adopted by it, and
- the extent of success achieved in this endeavour.

9.1 INTRODUCTION

A study of the economic development of pre-revolutionary Russia is very important not only because it makes it possible to discern more clearly the long-term trend of economic growth and facilitates a more accurate understanding of the developments in the country. Such an understanding is moreover necessary for assessing the achievements of different generations, and in the case of Russia in particular, for assessing the claims of adherents of two antagonistic and mutually exclusive socio-economic systems.

There are different views regarding the development of events in Russia. The supporters of Russian socialism claim that it was their policies that transformed a backward agrarian country into a modern agro-industrial State. On the other hand there are those economists and other social scientists who do not agree with such an assessment of Soviet achievements. They adhere to the view that during the period preceding the 1st World War and the Revolution enough groundwork had already been done in terms of reform of the economic system and formation of progressive capitalist relations, which would have, given the time, produced results no less spectacular than those achieved under the Soviet system. No clear answer has emerged, but a proper study may motivate someone to further study this problem and shed some new light on it.

9.2 BACKGROUND

The Emancipation Act of 1861 was an event of great historical import. Its terms

determined the procedure by which the peasant could become a legal and independent landholding entity and ceases to be a serf—a mere appendage to the land owned by the landlord. However, differences in agricultural activities as well as differences in the pattern of organisation of agriculture in different regions of Russia created a situation in which the impact of the Emancipation Act on various sections of the rural population and their inter-relationships were far from uniform both in terms of degree and breadth. Therefore, if we have to reach a correct understanding of post Reform agricultural development and the new problems the peasantry had to face during this period especially towards the end of the nineteenth and the beginning of the twentieth century it is necessary to take note of the peculiarities of at least the major agricultural regions of Tsarist Russia.

The north of European Russia is the region where most of the area was covered by forests or marshlands. The remaining area, not very large by itself, consisted of meadows and pasture lands. Just a very small portion was used for the cultivation of crops with the chief grain crop in this region being rye and not wheat. In this region due to its peculiarities (difficult drainage, long winter period, land largely unsuitable for ploughing, etc.) more progressive methods of land utilisation and cultivation were adopted than in other regions of Russia and the use of multiple grass crop and roots was introduced to improve upon the three field rotation system.

The central region consists of a belt that stretches from the district of Minsk in Bylorussia through Moscow to Perm in the east. The main form of agricultural activity in the region of this belt which lies between Minsk and Moscow were pig breeding and stock raising on a small scale, crops such as flax and potatoes (on a larger scale) and in very limited scale cereal cultivation. Around Moscow market gardening, dairy farming and cattle breeding were the most prominent forms of agricultural activities. To the east of Moscow the arable area comprised 50 per cent of the total land mass of this region. Most of the arable land here was occupied under rye cultivation and rest under some other cereals. Lifestock breeding was also conducted on a moderate scale. Further east towards Perm forest and pasture land occupied most of the area with arable land constituting only a small portion adequate, perhaps, only for purposes of rural consumption. This was thinly populated in contrast to the rest of the Central region.

The southern region : This was the black soil region, however, with largely unfavourable climatic conditions viz., greater extremes of summer and winter temperatures, lower rainfalls and winter precipitation. It was also characterised by low crop yields and extensive arable cultivation. Here the principal method of cultivation consisted in ploughing and sowing of the fields for as long a period as it was possible to obtain even a small yield. When further utilisation was rendered physically impossible due to complete exhaustion of the land, cultivation was shifted to fresh lands and the used ones were left for grazing.

Though this method prevailed in general for a long time, but with an increase in population pressure on land with time it became necessary to adopt more progressive methods of crop cultivation. Thus a method similar to primitive crop rotation came to be accepted here. Adoption of this method, the resulting expansion of arable area and a relative shrinking of pasture land was also caused by the increasing exports of grain from this region. On the eve of the 1917 revolution this area had already evolved into a region of extensive wheat cultivation for export purposes through the outlets provided by the Black Sea and Azov Sea ports.

The Siberian region is usually divided into two parts—the west and east. In western Siberia only the black soil zone which stretches from the Urals to the river Yenisei is suitable for cultivation, the rest of the region being covered by forests right upto the northern fringes. Unfavourable climatic conditions—lack of moisture, severe winter temperatures and inadequate depth of snow neutralise the natural richness and fertility of the soil. In parts, though, there are rich meadow lands in the valleys and foothills of the Altai. Here the prevalent methods of land utilisation were primitive, similar to the land exhausting method used in the southern black earth region. Only in a small area in the west of Siberia where the three-field rotation was in the earlier stages of being adopted, cattle rearing, dairy farming and wheat cultivation were the main forms of agricultural activity.

9.3 AGRICULTURE

In this section you will see how the agrarian scenario of Russia changed during 1861-1916. You will see the development of the nascent capitalist tendency in Russian agriculture, starting from an extremely feudal relationship in production structure.

9.3.1 Emancipation Act and Its Consequences

The Emancipation Act of 1861 marked the beginning of a new era in the history of social relations in Russia in that it imparted a new impetus to the development of capitalism and brought about a steady decline of feudal relationships (characterised by bonded labour-landlord relations) in the agrarian sector not only in the relatively developed parts of the country but also in those which had not witnessed even a moderate development during the preceding years.

It is only natural that the process of systemic change, due to social, political and economic complexities of a vast multiethnic Imperial State could not proceed in a smooth and painless manner, without contradictions and antagonisms. Historical events of later years showed that the process of ushering in changes in the structure of agrarian relations was fraught with problems. There were a number of reasons of why these problems caused deep dissatisfaction in the countryside among the rural population and caused widespread unrest.

The 1861 Settlement divided the land between the landlords and the peasants which went against the overwhelming opinion of the peasantry which believed that all the land belonged to the peasants as they were the ones who worked on the land. The peasantry came to consider the landlords and the gentry as a class of parasitic elements living off its labour while the peasants themselves were reduced to a state of virtual slavery. The peasants, therefore, right from the initial stages, did not accept the legitimacy of land ownership by the gentry and demanded that all the land should belong to those who work on the land and put it to productive use. Hence the peasantry did not agree with the basic idea of the Settlement of dividing the land between these two classes, and came to consider it as a scheme to deprive them of land which legitimately belonged to them.

Another reason that created massive discontent among the peasants was that this land, on which they have worked for generations and believed to have legitimately belonged to them, was not being actually restored to them, but was being sold to them in reality i.e., they had to buy out their share of the land, albeit in instalments over a long period.

Added to this sense of being cheated of their legitimate rights, of insult at what they believed to be a great historical injustice in restoring the rights of the peasantry was the fact that the Settlement did not in real terms provide equality before the Law to the peasants or true personal freedom. By the provisions of the Emancipation Act the land was to be held not personally by the peasant but by the village community, an institution called 'mir' or 'obshchina'. Apart from a few exceptions, land utilisation in Russia was controlled generally by the heads of the family in villages and it was regularly re-distributed at certain periodic intervals within a three-field system.

Another cause that indirectly intensified the feeling of having been denied their due was the fact that the payment of taxes and the redemption dues was made the responsibility of the villages, which naturally led to a situation where individual migration of the peasants from the villages to towns or other areas was restricted as the villages would not allow individuals to leave. By this measure the peasant continued to be practically restricted to his village, just as he was before the Settlement. As a result of this immobility of the peasant, population in the villages continued to grow at a rapid pace thereby putting a great strain on the means of subsistence. The rural population grew from 55.3 million in 1863 to 82.1 million in 1897 and, as estimates show, continued to grow at a rate which produced a growth of 20 per cent in 14 years between 1900 and 1914.

These, however, were only general trends and as we are going to see they did not have uniform application and instead the forms in which they manifested themselves in

universal tendencies as there were many exceptions and purely regional specificities.

Thus for different regions of the country the proportion between the peasants' share of land, landlord's holding and individual peasant holding showed significant variation. The Emancipation Act envisaged that serfs would be given possession, at a price, of almost the same amount of land which they had occupied previously. But now as the serf was no longer under obligation to work for the landlord on his field he was supposed to pay a certain amount annually to the landlord in order to compensate for the services of which the latter were now deprived. Hence the price to be paid by the peasant as **redemption due** was not only for the portion of the land allotted to him but also a price for redemption of his previous obligations to the landlords. The redemption dues were supposed to be paid over a period of forty nine years. The procedure adopted for such payments was that while the peasants paid their redemption dues—the capital amount plus the interest—to the State in annual instalments over the above mentioned period, the State on its part compensated the landlords by issuing interest bearing bonds immediately. A certain amount of flexibility was built into this system of settling the transactions by providing for a maximum and minimum limit on the amount of land to be allotted. These limits were quite different for different regions and within these limits settlement negotiations could take place between the landlord and the peasants and a choice could in principle be made between larger allotment of land for a larger amount to be paid as redemption due and smaller allotment of land for a smaller redemption amount. The redemption payments were also to be made in addition for the obligations that the peasant avoided towards his previous master. Therefore, the amount of land which was factually allotted to the peasant was relatively smaller than the redemption payment. It was one of the reasons which prompted the landlords to keep the allotment of land nearer the minimum rather than maximum limit. This characteristic also made the burden heavier for the peasant in terms of real material gains proportionally to the price paid.

There was also a provision for another type of land settlement whereby the peasants could forego completely payment of their redemption due if they settled for accepting only one-fourth of the standard allotment. These allotments were commonly known as '**poverty lots**' or '**beggar's allotment**' and provided the land owners with a very good opportunity of gaining possession of a part of the land which should have belonged to the peasants. This type of settlement transactions were very profitable for the landowners in areas where the price of the land was high and cheap wage labour was available. It was particularly in these areas that this type of settlement was frequently forced upon the peasants by the landlords.

Though statistical data shows that on the whole the amount of land that was allotted to the peasants was only marginally smaller than the amount they had held previously — all in all only by a margin of 5 per cent — but if we examine the regional differences we see that they were at times quite substantial. In the northern region, where as we have seen earlier, the conditions were not conducive for purposes of crop cultivation, the general tendency was to allot large portions of land for heavier payments for the uneconomical land under crop cultivation, while the landlords continued to retain in their own hands the more profitable pasture and meadow lands. The individual holdings were larger here, but the peasants were left to utilise the relatively uneconomic land which tilted the balance away from the latter. The redemption dues to be paid to the landlord were larger here than the market value of peasant land by a margin of two hundred per cent.

In Siberia where there had never been serfdom, independently owned farms had developed long before the 1861 Settlement and it was not uncommon here for the peasants to leave their villages in spite of the fact that many legal hurdles were put on their movements. Many peasants managed to amass considerable wealth thus giving rise to a class of rich farmers, even if their number was not very large. Here the land had always been Crown land; in other words it belonged to the Imperial State and was granted to the peasants in the late eighteenth century as a grant, to be used in perpetuity. Thus here the conditions of the peasants was not effected by the change — they continued to occupy the same amount of land after the Emancipation Act as they had occupied earlier with no significant change in their legal status as landholders.

In the black soil area of the southern region where the land was rich and fertile, the

their land as possible. So here they reduced the size of the land allotments to minimum while at the same time the redemption dues were also kept smaller. Forcing of the beggars' lots on the peasants was also a very frequent practice in this region.

9.3.2 Post 1861 Agricultural Development

Commercial agriculture though quite developed in many areas even before the Emancipation Act was greatly accelerated in the post settlement period. The main tendency for agriculture was to export grain to the foreign market instead of orienting its produce towards the requirements of domestic consumption. As it is pointed out by many authors, Russia's agriculture combined features that are more appropriate for grain importing country than for a country exporting grain. Relative smallness of arable area on the one hand, and low level yield on the other, and low level of per capita grain production are some of these characteristics.

Though Russia has fertile soil for grain production there are other factors that offset the benefits. These factors are both climatic and socio-economic in nature. We have already pointed out some of them earlier, but in addition to those mentioned such as inadequate level of precipitation, extreme cold or difference between winter and summer temperatures, one of the major natural causes of low productivity of agriculture in Imperial Russia was soil erosion. Most of the soil erosion occurred due to a rapid running off the melting snow at spring time. Instead of getting soaked into the ground, the water would run off taking the upper soil along with it.

Another cause for low productivity of agriculture in Russia was obsolete land utilisation technique : in most parts of the country one third of the land was allowed to lie fallow as the three-field rotation system was dominant in almost the whole of the country. In the rest of the areas even more primitive methods were in use. One such method was known as 'perelog' by which only a very small portion of the land was allowed to lie fallow leading to complete exhaustion of the land under cultivation after a certain period.

Pattern of land holding was also one of the major causes of low productivity of Russian agriculture. No proper balance was maintained between arable, pasture and haylands. An unfavourable balance of pasture land led to a shortage of livestock, and consequently to a shortfall in the availability of manure in adequate amounts. Since it was livestock manure which was mainly used to supplement the decreasing fertility of land due to obsolete land utilisation techniques, a shortage of manure resulted in low productivity of land. In the northern region where the land was not very fertile, the landlords managed to retain the more fertile meadow land at the time of the Settlement. So the peasants were deprived of the means of maintaining a large enough number of animals. The situation would become particularly acute during the winter months when it was impossible for the peasants to graze their animals in the forests due to a thick layer of snow. As the animals were practically deprived of food it was quite common for the peasants to slaughter them in the winters. It is estimated that usually during the winter period about one-third of the livestock would get slaughtered. In the south, on the contrary, where the arable land was more fertile and profitable the landowners had managed to keep large portions of the land thereby reducing the peasants' holdings proportionately. As this was the region of high population density so the peasants' holdings were the smallest, thereby reducing the capacity of the peasants to maintain large number of animals.

Apart from this the system of redistribution of land among the community members to which the village communities resorted periodically was conducted in such a manner that the land was held by an individual in strips which were usually scattered at long distances from each other. Not only that the strips were scattered, at times they would be situated at very long distances from the village itself. Considering the fact that on an average each household would hold upto 20-30 strips and occasionally even 100, it is easy to imagine how difficult it would have been to cope with the work during the extremely busy sowing and harvesting time.

The Settlement as we have seen resulted in polarisation of wealth and resources in the countryside, where a thin layer of wealthy and well-to-do farmers had emerged while the majority of the peasants continued to eke out a hand to mouth existence from

in Russia. The peasants made use of very primitive tools and implements of production. It is estimated that even in the post Emancipation period more than half of the peasants continued to use wooden ploughs; almost all over Russia sowing was conducted by hand; the threshing process was also carried out by hand. Estimates relating to the period under consideration show that on an average only one reaper and threshing machine was available for every 25-30 farms. Only well to do 'kulak' class of farmers were in a position to take advantage of modern farming technology and it was precisely on these farms that the yield was generally higher than the average. It was also here on larger estates that cultivation of specialised crops for selling in the market was developed. It was oriented towards both domestic, urban and foreign markets. Though the large estates accounted for a third of the total agricultural produce, they had a major share in the marketed surplus. The small farmers and peasants would sell only a small portion of their produce which would be sufficient to pay their debts, dues and taxes as well as for procuring certain necessary products from the urban market. The majority of the peasantry was nothing more than subsistence farmers, carrying on their agricultural activities on small plots with the help of primitive implements.

Thus the problems of the countryside were manifold and complex, and discontent in the countryside reached a peak during the last decade of the nineteenth century. Many proposals were put forward and discussed by the Tsarist government but no real and effective corrective measures were adopted to stem the rising discontentment in the countryside. In the end it was the shock of the 1905 revolution with the widespread uprising and land seizures that made the government realise that immediate and radical reforms were needed and any further delay was fraught with dire consequences for the country and the system of Monarchy.

9.3.3 Reforms of 1905 and 1910

This realisation was at the basis of the reforms of 1905 and 1910 which were carried out by the Tsarist minister P.A. Stolypin. The most outstanding feature of this reform was a measure of breathing space and relief given to the rural poor especially poor farmers by abolishing all further payments of outstanding redemption dues. Another major achievement of this reform was that the peasants were now allowed to leave their respective communities in their villages; they could now buy or sell their land according to their own desire; migrate to the cities or to other regions. The Stolypin reforms were a major milestone in the evolution of social relationships in the country as a whole and in the countryside in particular, as it facilitated a major rearrangement of traditional agriculture, considerably strengthening a prosperous peasant class, a class of proprietors which could now be considered to become a loyal ally of government and Monarchy. The government met significant success in its endeavour as about twenty four per cent of the households in European Russia left their communities and established their own independent and privately owned farms, which came to approximately 2 million households in 1916.

This was a period of rapid growth of commercialisation of agriculture and capitalist relations both in 'depth' and 'breadth'. The progressive elements were now using modern agricultural equipment leading to a greater efficiency of agricultural production. Net agricultural income rose sharply by 88.6 per cent during the period 1900-1913, which meant an increase of 34 per cent in output in constant prices. Export of grain also showed remarkable increase during the period 1900-1913 — they exceeded the 1905 level on an average by 50 per cent.

However, the positive impact of these reforms was neutralised by two factors. Firstly, the reforms did not have redistribution of the land owned by the church and the landlords as its objective. As a result of this their land was left untouched by and large. Thus the main grievance of the peasants was not removed. Secondly the reforms did little to help the poor peasants to improve their lot, except for the fact that they were now free to sell their land and move out, a practice to which a large number of peasants resorted as a desperate attempt. This led to a swelling of the ranks of the landless peasants in the countryside and those of wage seekers in the urban areas. In any case the reforms brought little relief to the mass of the population and only increased the hostility of the majority of the poor classes towards the well to do sections in the country.

for crop production on Goldsmith's index, where the 1896-1900 level is taken as 100, increased from 50 to 1861 to 140 in 1911-1913 showing an annual growth rate of 2-2.25 per cent on an average. Growth of livestock production similarly has been estimated at approximately 1 per cent per annum for 1860-1914 thereby keeping the overall agricultural annual growth rate at a meagre 1.7 per cent. There was hardly any increase in the per capita food consumption showing an insignificant 0.25 per cent increase per annum in per capita farm output including industrial crops and produce for exports. The productivity of agriculture grew as the following table show :

Table 9.1 : Growth of Agricultural Productivity : 1860-1910

Country	1860	1910
Germany	10.5	25.5
Belgium	11.0	18.0
Spain	11.0	8.5
USA	22.5	42.0
France	15.5	17.0
Italy	5.0	6.5
UK	20.0	23.5
Russia	7.5	11.0

Source : (Nove. A. An Economic History of the USSR, p. 24)

Thus Russia over a period of 50 years could only overtake Spain; it grew at a faster pace than Great Britain and France but slower than USA and Germany.

Check Your Progress I

- 1) Name and describe the main agricultural regions of Russia.

.....

.....

.....

.....

.....

- 2) What were the major changes ushered by the Emancipation Act?

.....

.....

.....

- 3) Name the factors responsible for low productivity of Russian agriculture.

.....

.....

.....

.....

.....

Which of the following statements are true :

- Commercial agriculture was widespread in post Emancipation Russia.
- Use of modern technology was common.
- Standards of life in the countryside were high on an average.
- There was a migration of workers from urban centres to the countryside.

- 5) Say whether the following statements are true or false:

- The 1905 reform distributed the land of the church among the peasants.
- There was no substantial improvement in the living standards of the peasants after 1905.

- d) Russian agriculture grew faster than that of Germany in the Long-term perspective.
- 6) What were the positive points in the Reforms of 1905 and 1910?
.....
.....
.....
.....
.....
- 7) List the positive effects of these reforms.
.....
.....
.....
.....
.....

9.4 INDUSTRIAL DEVELOPMENT IN PRE-WAR PERIOD

During the period of more than half a century between the Emancipation and the First World War Russia witnessed significant changes not only in the agrarian sector and rural areas but also industry, education; social relations in urban centres underwent qualitative change.

Industrial development in Russia was begun in earnest as early as the reign of Peter the Great in the early eighteenth century. Industrial development was an important element in the great design of 'civilising' Russia undertaken by Tsar Peter and forced upon a reluctant nobility and populace in general. Peter the Great, who had travelled extensively over Europe was greatly impressed by its technological achievements and it must be said to his credit that he realised that if Russia has any chance of becoming a major power capable of successfully competing with the European nations it has to outgrow the predominantly agrarian character of its feudal economy. Thus he set about to determinedly industrialise Russia 'from above' primarily by importing technology and scientists from Europe. In his design of things military considerations were certainly not at the bottom. However, it must be said that Peter the Great while industrialising Russia was not attempting to replace feudalism as socio-economic system. On the contrary during his regime feudalism got entrenched even more firmly and Absolute Monarchy became indisputable.

However, the situation changed after the death of Peter the Great and the pace of industrialisation began to peter out leading to an ever increasing gap in the level of industrial development in Russia and that of the European countries. By the middle of the nineteenth century Russia had already fallen far behind the contemporary level of industrial development in European countries.

9.4.1 Emancipation Act and Industrialisation

The defeat of the Russians in the German War and the complete failure of its military came as a great shock both for the people and the ruling classes. It forced upon them the realisation that theirs was an economically backward and hence militarily weak country, a realisation which was instrumental in finally bringing about the abolishment of serfdom through the Emancipation Act. Along with this came the realisation on the part of the Government of the necessity of industrialisation, though not without initial doubts under conservative influence. But with time industrialisation came to be consciously pursued by the government.

1890-1905 during the tenure of Count Witte as the Ministry of Finance.

The government encouraged industrial development in the country in a variety of ways :

- i) The State sponsored massive railroad development especially between major economic regions of the country;
- ii) The State acted as the guarantor of bonds, thereby encouraging foreign capital to flow into the country in a big way;
- iii) The State took active measures for recruitment of foreign entrepreneurs to operate in the country.

The State practically substituted for the missing entrepreneurial class in the country. The active role of the government in promoting industrial development in a wide variety of ways produced excellent results and was one of the main causes of the spectacular spurt in industrial growth during the 80s of the last century.

Table 9.2 : Index of Industrial output (manufacture and mining) (1900 = 100)

1860...13.90	1896... 72.90	1905...98.20
1870...17.10	1897...77.80	1906...111.7
1880...28.20	1898...85.50	1907...116.9
1890...50.70	1899...95.30	1908...119.5
1891...53.40	1900...100.0	1909...122.5
1892...55.70	1901...103.1	1910...141.4
1893...63.30	1902...103.8	1911...149.7
1894...63.30	1903...106.6	1912...153.2
1895...70.40	1904...109.9	1913...163.9

Source : Nove. A. An Economic History of the USSR, p. 12.

According to Goldsmith's estimates, as it has been cited by A. Nove, industrial output in Russia grew at a rate of 5 per cent per annum between 1888 and 1913. Such a growth rate is higher than that of the USA or Germany on a per capita basis. Soviet estimates also show remarkable growth in industrial production over the period 1860-1910. According to these estimates industrial production in Russia over the above mentioned period increased by 10.5 times, whereas the similar indicator for the world was 6, for Germany 6 and Great Britain 2.50.

However, the most widely held opinion is that Russian industrial development, in spite of considerable achievements in area compared to the earlier period in the country, was not enough in its bid to catch up with the progress made by the advanced countries of the world. When growth rates are taken in percentage terms Russian industrial development can be considered to be quite commendable, but when compared to the immense resources that were at its disposal and the gap that still remained between Russia and the developed countries it becomes obvious that industrial development was in essence inadequate.

Table 9.3 : Relative Industrial Progress of World Powers 1860-1910

	Raw cotton (Kg. per head)		Pig iron (Kg. per head)		Railways *		Coal (Kg. per head)		Steam power (h.p. per 1000 person)		Ranking list		
	1860	1910	1860	1910	1860	1910	1860	1910	1860	1910	1860	1910	
Germany	1.4	6.8	14	200	21	75	400	3190	5	110	130	6	4
Belgium	2.9	9.4	69	250	30	102	1310	3270	21	150	2	3	3
Spain	1.4	4.4	3	21	6	58	330			4	8	8	8
U.S.A.	5.8	12.7	25	270	19	122	420	4580	25	150	180	2	3
France	2.7	6.0	25	100	18	87	390	1450	5	73	5	5	6
Italy	0.2	5.4	2	8	6	38	270			14	46	9	10
Japan		4.9		5		14	230			7	10	11	11

Economic Development of Russia-1

Russia	0.5	3.0	5	31	1	24	—	300	1	7/16	9/10	10
Sweden	1.5	3.6	47	110	3	76	90	910	—	55/150	7	7
Switzerland	5.3	6.3	—	—	28	88	—	—	—	85/190	4	4/5

★ Total length related to population and area.

† The higher figure includes other forms of power.

— Negligible or not available.

Note : Most figures represent an average over several years.

Source : A. Nove. op. cit. page 16.

Industrial growth was quite rapid in certain periods but in other periods it failed to maintain the same momentum and would fall back. During the period 1891-1900 industrial production more than doubled and particularly the heavy industry showed remarkable advance. Railway construction, oil production, iron and steel industry showed remarkable rates of growth during this period. During the period 1900-1905 there was a significant slowdown in the rates of industrial development due to the economic crisis. In the following two years there was a moderate recovery, but then the rate of industrial growth again showed a slowdown. This slowdown seriously affected heavy industry especially iron and steel industry. This industry reached the 1900 level only in 1910. After this the Russian economy showed a sharp rise right upto the outbreak of the First World War. Therefore, one of the most striking features of the post Emancipation development of the industrial sector in Russia was its uneven development when viewed in terms of the time factor.

The development of the industrial sectors in Imperial Russia was not only uneven in time but also it showed a remarkable unevenness geographically i.e., the different regions of the country showed varying rates and levels of industrial growth in the post Emancipation period. The surrounding areas of the St. Petersburg and Moscow districts and the coal rich regions of Ukraine showed remarkable progress both in terms of quantity and quality. It was in these regions that the rate of industrial growth was highest with the largest and well equipped enterprises comparable to those in the development countries. Ukraine in the south was evolving as the principal metallurgical centre of Russia which provided this sector with the benefits of proximity to two vital inputs—fuel (coal) and raw material (iron ore) which were to be found in abundance here. Plentiful sources of cooking coal are in the Krivoi Rog region about 350 kilometres to the west. Exactly due to a lack of these resources in the region that the old metallurgical centre in the Ural mountains was now in the process of steady decline. Most of the remaining territories had little to boast about any significant increase in industrial production leave aside one based on modern technology. In most of these areas handicraft or 'kustarny' industry was prevalent. In addition the oil bearing Baku region in the extreme southern part of Azerbaijan, witnessed a certain amount of industrial development. Leading aside these islands of modern industry organised on a large scale and on modern principles of organisation, rest of the country, especially the southern and the eastern regions, were very primitive.

The industrial development in Russia was characterised also by a similar uneven development of different sectors of industry. Certain sectors of the industry grew at a much faster pace than the others. Thus Railway construction received priority. The Russian railway network which consisted of 1,600 km of tracks in 1860 was increased to 81,000 km in 1917. The Trans-Siberian railway by 1904 had linked up Moscow with the Pacific coast. The Central Asian town in Tashkent was linked to the Volga and to the Caspian Sea by a railroad track built through the Turmenian desert. In spite of this remarkable development the railway system in Russia continued to be inadequate and inferior when compared to the standard of railways prevalent in the countries of Europe. In many parts of the country the railway engines were using wood as fuel, the trains were slower and the tractive power of the locomotives was also lower. Russia ranked lowest among the European countries in railway development when compared in terms of the area and population.

The road development also followed a similar pattern, only that it can be characterised as being even more primitive. Though new road construction was undertaken it turned out to be grossly insufficient. Approximately 30 thousand

Heavy industry was also actively promoted by the government and was protected by a variety of measures such as tariffs & tax exemption and reductions, government orders at high prices and draconian police measures to keep labour under control. New iron and steel industry was developed at an impressive scale. The larger factories could employ up to ten thousand workers. What is more important in this case is not the scale but the establishment of capitalist monopolies usually in the form of cartels. The output of pig iron almost trebled during the period 1891-1900. In comparison the output of pig iron during the same period in Germany increased only by 1.6 times. The oil production during this decade also showed remarkable increase, and it grew at the same rate as the oil production in USA and even overtaking it in 1900 when it became the biggest producer of oil in the world. However, the oil industry failed to keep up the momentum in the following decade and showed a fall in the first decade of this century. While these sectors showed significant changes, other sectors and most notably the engineering sector continued to lag behind. Most of the equipment was imported. This lack of development of the engineering sector represented a major weakness of Russian economy and its dependence on imports of machines and equipment was the principal cause of many difficulties Russia was to face during the War. Small scale industry was an important part of the industrial structure. It consisted of about 33 per cent of the industrial output and gave employment to more than 5 million people or about 67 per cent of the industrial workforce. This sector included artisans and small workshops. The technological base and methods of production and its organisation were primitive.

This industrial development in Russia was characterised by unevenness— temporal, regional and sectoral.

As it has been pointed out earlier the Russian Government pursued a policy of attracting foreign capital by providing them exceptional incentives. Thus it is estimated that foreign capital constituted 28 per cent of the capital of private firms in Russia in 1900 and about 13 per cent in 1913. The increase of foreign investments in Russia for the same period is assessed at 85 percent while for Russian capital investments grew by 60 per cent. Thus, though domestic capital investments were rising at fairly rapid rate they were not able to keep pace with the inflow of foreign capital. Foreign investments were made in a variety of sectors but it was above all in the oil industry that the foreigners came to dominate. Foreign participation was also substantial in other sectors; 42 per cent in capital goods industry; 50 per cent in chemical industry; 28 per cent in textile industry and 37 per cent in wood working.

9.4.2 Overall Economic Development

The net national product of Russia grew relatively slowly during the first two decades after the Emancipation. But during the period extending from mid-eighties of the last century to the outbreak of the World War I the growth of the national income was approximately 3.3 per cent.

Table 9.4 : Rates of Growth of Different Economic Indicators (%) (1861-1913)

Period	NNP	Popl.	Per capita NNP	Labour Force	NNP per Worker
1861/63-1881-83...	1.8	1.1	0.7	1.9	0.1
1883/87-1909/13...	3.3	1.6	1.7	1.7	1.6

(P. Gregory. *Economic Growth and Structural Change in Tsarist Russia. Soviet Studies*, vol. 23, no. 1.p. 442)

If we compare the output growth of Russia in per capita and per worker basis it comes to about the average for the developed countries. But the above average growth of its output then was due to a more rapid increase in population and work force. The growth involved utilisation of growing inputs instead of growth per unit of input i.e., it was extensive in nature.

In the post emancipation period economic growth was also accompanied by structural changes in Russia's national income which show that in aggregate terms the share of the industry increased while that of the agriculture decreased. On the other

Check Your Progress 2

1) What were the measures taken by the Russian government to promote industrialisation?

.....
.....
.....
.....
.....

2) What were the main features of unevenness of industrial growth in Russia?

.....
.....
.....
.....
.....

9.5 LET US SUM UP

There is no doubt that the Russian empire had undergone rapid economic change. A new dynamic class of private entrepreneurs had been created both in industry and agriculture and new social relations were in the process of being established. Agriculture and industry had developed modern models of organisation and were growing. A large enough middle-class had been formed but it was still not able to stand on its own feet and give its aspiration a political expression.

But at the same time the change that was brought about by the adequate results and whatever change had occurred was very uneven both geographically and sector-wise. The gains of the reforms were limited to only a very small section of the population. The rest of the people were not satisfied with their conditions of living and their standard of life was appallingly low. Discontent was widespread specially among those who constituted the majority—the workers in the towns and cities, and peasants in the countryside.

Therefore, if we take into consideration only the quantitative changes then it may be surmised with a fairly considerable degree of certainty that with time Russia could well have evolved into a modern economic power. However, if we take into consideration the qualitative indicators of social antagonisms, popular discontent and desire for radical changes then it becomes very difficult to answer the question in the affirmative.

9.6 KEY WORDS

Allotment : The plot of land which a peasant could buy for a payment.

Crown land : Land belonging to the Imperial Government.

Mir : An institution of the village community formally for the purpose of deciding the matters concerning the village and its members.

Pereleg : Land utilisation method in which land was used for a long period until it got exhausted.

Poverty Lots : Plot equalling one fourth of the standard allotment for which no payments were required.

Serf : Peasant who is attached to the land of the feudal landlord.

9.7 SOME USEFUL BOOKS

Nove, Alec. 1969, *An Economic History of the USSR*. Penguin London, (Ch.1).

Gershenkron, A. 1968, *Russian Agrarian Policies and Industrialisation, 1861-1917* in "Continuity in History and Other Essays", pp. 144-147.

Gershenkron, A. 1962, *Economic Backwardness in Historical Perspective*, Harvard University Press, New York.

Dobb, Maurice 1960, *Soviet Economic Development Since 1917*, 5th ed. London.

Gregory, Paul 1981, *Economic Change and Structural Change in Tsarist Russia and the Soviet Union : A Long-Term Comparison*, in S. Rosefielde, ed., "Economic Welfare and the Economics of Soviet Socialism", Cambridge University Press.

9.8 ANSWERS TO CHECK YOUR PROGRESS

Check Your Progress 1

- 1) Read Section 9.2 to answer the question.
- 2) Read Section 9.3.1 to answer the question.
- 3) Read Section 9.3.2 to answer the question.
- 4) All the statements are false
- 5) a) and b) are false
b) and c) are true
- 6) Read Section 9.3.3 to answer.
- 7) Read Section 9.3.3 to answer.

Check Your Progress 2

- 1) Read Section 9.4.1 to answer.
- 2) Read Section 9.4.2 to answer.

UNIT 10 OCTOBER REVOLUTION AND ECONOMIC DEVELOPMENT : 1917-1920

Structure

- 10.0 Objectives
- 10.1 Introduction
- 10.2 Immediate Measures of the Soviet Government
 - 10.2.1 Major Decrees of the Soviet Government
 - 10.2.2 Organisation of Industry
 - 10.2.3 State Capitalism and Nationalisation
- 10.3 War Communism
 - 10.3.1 Background
 - 10.3.2 Productivity and Inflation
- 10.4 War Communism as an Economic System
 - 10.4.1 Economic Measures of the Soviet Government
 - 10.4.2 Centralisation
- 10.5 Let Us Sum Up
- 10.6 Key Words
- 10.7 Some Useful Books
- 10.8 Answers/ Hints to Check Your Progress Exercises

10.0 OBJECTIVES

After reading this unit you will come to know about :

- the specific compulsions and constraints under which the Soviet government had to operate and take policy decisions;
- the economic measures taken by the Soviet government during the period 1917-1920; and
- the nature, advantages and drawbacks of War Communism as an economic system.

10.1 INTRODUCTION

The Soviet system was not created in a vacuum, on the contrary it developed steadily as a long series of measures in response to the prevailing social, political and economic conditions and the objectives of the Soviet leadership.

One of the main characteristics of the economic system of War Communism was a very high degree of substitution of the market mechanism by a system of managing the economy through centralised directives. This fact has generated a lot of debate among the social scientists studying various aspects of the Soviet system. A section of the scientists believe that War Communism was a deliberate attempt on the part of the bolsheviks to usher in communism without delay. But another section of the scientists hold the view that War Communism cannot be viewed, as such, in isolation from the specific conditions of the time. The latter had acted as a constraining factor and many characteristics of War Communism, including centralised administration, were forced upon the Government.

Though there was a tendency on the part of a section of the bolsheviks towards directly ushering in communism, it must be admitted that the leadership and specially Lenin had not shown any such tendency.

A detailed study on this topic is necessary to get an insight to the complexities of economic development in this period. It will help in evolving a proper understanding, not only of the specific case of War Communism, but also of a more abstract issue of

10.2 IMMEDIATE MEASURES OF THE SOVIET GOVERNMENT

The Revolution of March 1917 went only half-way towards the main requirement of the time—demolishing the economic foundations of the nobility. Therefore the central concern of the Bolsheviks after the October Revolution was certainly not one of immediately embarking on a course of building a communist society, but firstly, of completing the unfinished tasks of the March revolution and secondly of preparing the ground for transitional stage from Capitalism to Socialism.

Even the second goal of the Revolution appears to have been not given the highest priority on the agenda of measures to be urgently undertaken. The Revolutionary leadership was at this point of time more concerned about bringing firmly under its control all those crucial economic levers and positions in the system which would allow them to consolidate their political power on the one hand, and on the other, to take hold of and retain under their control those sectors which were crucial for keeping the economy of the country from disintegrating.

10.2.1 Major Decrees of the Soviet Government

One of the first decrees to be issued by the Bolsheviks after coming to power was the **Land Decree of 8 November 1917**. The Bolsheviks had captured power only a day before and in concordance with their primary objective they set about depriving the feudal class of its economic base by nationalising the large estates and legalising the distribution of the nationalised land among the peasantry. This was an historic event in the sense that from now onwards for the first time in the history of the country the individual peasant was recognised as the proprietor of his own piece of land. He was now legalised as an independent economic entity who now had the right to make all the basic decisions regarding his economic activity. These decisions were : what to produce, how much of it to produce, what proportion to retain in his own hand for his personal and productive purposes and what portion of the produce to sell in the market in exchange for industrial goods.

Special note must be taken of the fact that for the Bolsheviks it was above all a political decision. The Bolsheviks had realised that by undertaking this long delayed measure they will be winning a new ally among the peasants. As we had mentioned earlier, the peasantry nurtured a deep sense of historical injustice by being denied all the land. They wanted all the land to be restored to them. By doing just this the Bolsheviks assured themselves of the support of the great mass of at least the rural poor and the middle farmers. Undoubtedly, this decision had as much political as economic significance.

Another major decision to have been taken by the Bolshevik government after coming to power was regarding the basic worker-proprietor relations in the industrial sector. It was decided that the workers must have greater rights in the functioning of their respective enterprises enabling them to exercise general control over the production process. The **Decree on Worker's Control** was passed on 14 November 1917. By the provisions of this Decree the functions, rights and authority of both the workers and their organisations on the one hand, and the rights and authority of the proprietors and the management on the other, were demarcated and specified. The workers were given the right to supervise the production organisation, determine the minimum level of production and to have full access to all the information concerning the enterprise's accounts and its business correspondence. At the same time the proprietors were given the power to conduct the day to day production process and direct the working of the enterprise. The workers and the Trade Unions were forbidden from countermanding the directives of the management or the proprietor. They were also forbidden from conducting voluntary takeovers of the enterprises without sanction from appropriate State authorities.

Nationalisation and confiscation of property and productive assets on a large scale, as we would see later, were resorted to much later and that too under exceptionally difficult circumstances and as an emergency measure for safeguarding the

The nationalisation that took place in the first months of Soviet rule was in fact carried out only for very specific reasons pertaining to the imperatives imposed upon the government by the unique conditions of the immediate post revolutionary period. Among the enterprises which were nationalised first, above all were those individual enterprises which were in one way or the other involved in the defence production providing armaments and other goods and materials for the ongoing war. These production units were of crucial importance for the government. Secondly those enterprises were nationalised where the proprietors had declared a lockout on one pretext or the other. Thirdly, enterprises, where the implementation of the provisions of the Worker's Decree met with hostility on the part of the proprietors who resisted its implementation, were nationalised. It was not until the summer of 1918 that full scale nationalisation of large sectors or the whole of the industries was carried out.

10.2.2 Organisation of Industry

Of much greater historical relevance are the experiments which were carried out by the government with an objective of creating new forms of organisation of production and which would be most appropriate to the new and qualitatively different requirements.

Mixed Companies

For some of the larger enterprises and for those which had a substantial participation of foreign capital the government put forward a proposal that the State and the private investors jointly manage the affairs of running the enterprise so as to facilitate the process of these enterprises evolving into a form of mixed companies. These proposals could not materialise at that time in spite of a series of negotiation rounds between the government and the representatives of leading entrepreneurs to create on experimental basis similar companies preferably with foreign participation in the metal producing industry for a beginning. Only much later when the New Economic Policy was introduced that this form of organisation of industrial production could be established.

Centre

Another organisation to have been established during this period was that of the 'Centre'. This form was instituted mainly in the light industry where private and government owned enterprises continued to exist side by side. These centres were conceptualised as controlling bodies which were given the power of regulating and exercising general control. All the parties—private businessmen, trade unions and the Government—were given adequate representation in the composition of the centres. There was no fixed number (quota) of representatives from each side and this would differ from case to case depending on a number of factors. But usually about half of the overall members were supposed to represent the trade unions and the other half would usually consist of equal number of representatives of the government and private owners.

The centres were given the authority to :

- i) regulate the distribution of stocks and materials;
- ii) regulate the prices of the products within the area of their competence;
- iii) determine and oversee the merger of various enterprises;
- iv) regulate nationalisation of any enterprise if need arose.

There was also a provision enabling the centres in very specific cases to exercise their rights to :

- i) take over the supply of basic resources—raw materials and fuel—to various enterprises within their own industry;
- ii) market the produce of an enterprise belonging to their branch of industry;
- iii) exert a monopoly on export and import operations of the enterprises belonging to their branch of economy;
- iv) draw up plans for purchase, quality control and distribution of products;

The function of control by the government over the production process in the various sectors of the heavy industry was exercised mainly through the organisation of 'Glavki' falling under the competence of 'Vesenkha' or the government's Supreme Economic Council. The status of the 'glavki' was that of a 'department' in the Vesenkha structure. Glavki were plenary organs of the government with the same powers on a scale limited to their respective spheres as those which the Vesenkha exercised on the scale of the economy as a whole. The 'glavki' constituted a more direct and centralised form of governmental regulation of industrial production when compared to the 'centre'. Contrary to the objectives of joint management of the 'centre', the 'glavki' were constituted with the specific purpose of coordinating the activities of 'Workers' control' committees and of helping the authorities in proceeding with nationalisation in a systematic manner. This meant passing on to the 'glavki' functions like : acquiring exclusive rights of exploration of new resources in case of raw materials, control over private companies, establishing new companies, distribution of the product of companies belonging to their branch of industry, shutting down technically obsolete enterprises, formulation of production plans (defining output targets), transport and delivery schedules, determining wage scales for different categories of workers and employees, distribution of inputs etc.

The managing body of these 'glavki' consisted of representatives from the government, Trade Unions and a team of technical experts, the latter purely in the capacity of an advisory group.

10.2.3 State Capitalism and Nationalisation

One of the most widely debated problems of the post revolutionary economic development in Russia concerns the question of nationalisation. Was the nationalisation wave that followed the ascendancy of the bolsheviks to power a conscious long-term policy decision of the government, or was it a crisis response on the part of a beleaguered and unstable government?

Many prominent authors and students of Russian economic history hold the opinion that though accelerated nationalisation appears to be the most outstanding phenomenon of the first decade after the revolution, it is absolutely necessary to identify two well demarcated stages in progression of this phenomenon—the earlier eight-month phase which began with the bolsheviks coming to power and ended in June 1918; the second phase which began immediately after when large scale nationalisation was effected as a means of 'expropriating the expropriators'. The first phase is seen as a crisis response on the part of the government on the one hand, and manifestation of anarchical tendencies among the workers on the other. This was a far cry from a conscious, pre-planned effort at extensive socialisation of the country's economy. In contrast, the second phase which began after the summer of 1918 was undoubtedly a part of a pre-conceived long-term policy.

The government had to resort to large scale and forcible nationalisation after June 1918. This indicated that its attempts to limit direct takeovers to a minimum number of enterprises and exercise control by means of economic organisations like 'centre' and 'glavki' were unable to survive the pressures of the existing political conditions.

Two basic reasons are put forward in explaining the failure of the government to pursue its course of compromise and gradual transition, its failure to build up on its achievements in developing State Capitalism characterised by 'joint' management of the economic and productive activity.

The reasons for the government's failure are seen in the excessive revolutionary zeal and uncoordinated initiatives of the workers and their organisations—trade unions and the local Soviets. It was not uncommon for the factory committees to take over the administration of their enterprise without approval from higher authorities in defiance of specific directives from the central bodies refraining the factory committees from taking over the administration as it was beyond the powers accorded to them by the Decree on Workers' Control. The usual practice was that the workers would break into the office of their enterprise and declare that they are taking over

reality. Such cases were not by all accounts isolated phenomenon. On the contrary one can consider it to be a trend characteristic of the period. There was a marked tendency on the part of the factory committees towards such illegal takeovers of the administration of their enterprises. This tendency was sought to be justified on the ground that all productive assets in the country must belong to those who work on it: factories to the workers as land to the peasants. The tendency that these factories must be run by the workers of this or that factory above all for their own benefit came to be known by the name of 'syndicalism'. Syndicalism proved to be an extremely negative phenomenon resulting in gross indiscipline among the workers. It led to chaos and decline in production and often pitted one section of the workers against the other. The rise in sectarian interests among the workers was seriously undermining the larger interests of the class and the revolution as the workers tried to oppose any kind of coordination of their activities with outside agencies as it usually meant compromise and acceptance of outside advice or directions.

Any organisation of the production process on a large scale or any systematic restructuring of the industry and other sphere of the economy was practically impossible by the syndicalist tendencies among the workers. Moreover, such tendencies were limited not only to the workers. Among the bolsheviks too there was a section of extreme left who did not like the management of the factories to be run by professional managers. At the Third Congress of Trade Unions the bolsheviks' demand of introducing scientific management procedures in the factories was met with a lot of hostility and opposition and was labelled as 'heritage of capitalism' and 'remnants of capitalist exploitation' etc.

Check Your Progress 1

1) Which were the two major Decrees issued by the Soviet government immediately after the October Revolution?

.....
.....
.....
.....
.....
.....
.....
.....

2) Say whether the following are true or false :

- a) Nationalisation was massive after the October Revolution. (True/ False)
- b) Nationalisation was a deliberate policy. (True/ False)
- c) Only selected enterprises were nationalised. (True/ False)
- d) Workers wanted to leave the enterprises with their owners. (True/ False)

3) Describe the new forms of organisation of industrial production created by the Soviet government.

.....
.....
.....
.....
.....
.....
.....

- b) Nationalisation was massive after June 1918 (True/False)
- c) Takeovers by the workers were rare. (True/False)
- 5) What were the reasons for the failure of the Soviet government to pursue a gradual course of economic reforms?

.....
.....
.....
.....
.....
.....

- 6) What was 'syndicalism'?

.....
.....
.....
.....

10.3 WAR COMMUNISM

One of the most neglected points on War Communism as an economic system is that this system did in the end prove to have played a crucial role in the victory of the bolsheviks in the civil War against incredible odds. But this kind of success of the system of War Communism, once admitted, must not deter us from asking an even more basic question : whether or not War Communism, in historical perspective, can be considered a viable economic system which was capable of solving long-term economic problems facing the bolsheviks in the twenties of this century.

In order to answer this question we will have to conduct a proper evaluation of the system in terms of how different sectors and other participants in the overall economic arena responded to the policies of the government, and to what extent this response coincided with the expectations of the policy makers. Finally, we would like to know whether the functioning of this system led to a consolidation of the economy or to disruption of the vital links between various sectors of the national economy. However, any exercise with such an objective will have to include a proper evaluation of the concrete historical conditions prevailing during the period under study, and of the events leading to adoption of this or that policy by the leadership of the country.

10.3.1 Background

These conditions, as far as the economy is concerned, could not have been worse for any government in the world, even for those best placed to tackle them. The Soviet government had lost most of its territories to a host of armies fighting against the revolutionary regime. In the north General Yudenich stood at the gates of Petrograd; the British were in control of the extreme north with the British navy laying a virtual blockade at the entrance of the river Neva into the Gulf of Finland, thereby cutting off an important water transport route. The east was under the White armies of Admiral Kolchak and the Czeks and the rebellious Czek. The whole area in the south from the sea of Azov to the volga was occupied by the forces under the overall command of General Denikin.

The resulting shortage of raw materials coupled with a severe disruption of the food supplies had a crippling effect on the economy, exacerbating further the disorganisation and administrative chaos that had been created in the wake of workers' anarchy and syndicalism of the first eight months of Soviet power.

In the south the White armies were in control of the crucial coal rich area of

production in 1913. The supply of these crucial inputs was now effectively cut off. The other pig iron producing region of the country was also cut off from Moscow by Admiral Kolchak and the Czeks. As a result the production in those metal producing units which were still in the central Soviet held area was drastically cut down depriving the ammunition industry and engineering sector of crucial inputs.

Coupled with it was the stoppage of supply of oil from the Baku region. The Soviets found themselves being deprived of it. This created a fuel crisis which resulted in converting the railway to the use of wood as fuel. The inability of procuring fuel and metal led to repairs being not done on time or not at all, thus disrupting the already decrepit transport system. An idea of this transport crisis can be had from the fact that only about 50 per cent of the locomotives in working condition were being used for purposes other than military. About 47 per cent of locomotives were standing idle at the end of 1918 for want of repair. The government was able to avail of less number locomotives with time—there were about 14,500 locomotives in the hand of the government in 1917 but by the end of 1918 it could make use of only 5000 and about 20 per cent of railroad wagons were also not available due to want of repairs. The Soviets had lost almost 60 per cent of their railway network to the Whites.

10.3.2 Productivity and Inflation

Under these conditions the productivity of industrial production was bound to have been affected. A situation was created where there was a lot of chaos in the administrative system which was unable to cope with the magnitude and complexity of the situation. Added to this was the acute shortage in food supplies to the cities. This had a very demoralising effect on the workers. It grievously lowered their capacity to work with the required intensity and affected their capacity to regularly attend work, as virtually starvation and semi-starvation conditions made them physically weak. There was also a spurt in petty thefts and robberies. It is estimated that the average productivity of workers was reduced by almost 65 per cent in 1920 with absenteeism reaching a level of about 60 per cent at its highest and remaining at a considerable level of 30 per cent most of the time.

Under such extreme conditions of (i) shortage not only of materials and fuel, but also of food products and other necessities (ii) an acute shortage of workforce due to physical inability to work (iii) recruitment of a large number of workers for fighting at the various fronts (iv) migration of a large urban populace to the country side to escape from the hardships of city life and (v) the heavy strain put by the war on the finances and the government's incapacity to augment the same, made it impossible for the government to tackle the problem of inflation in an effective manner. Some effort was made on a very limited scale to tap extra financial resources by mainly targetting the rich city dwellers and businessmen by slapping extra levies on them. But in the given circumstances the possibility of raising revenue through this method was very limited and absolutely inadequate. Thus the government was not left with any alternative other than resorting to printing more money.

One of the reasons that forced the government to resort to printing more and more money was that in an economy where shortages have become endemic and chronic it was the only way by which the government could augment its reserves. This means that inflation helps the government to acquire more resources than it would have otherwise. In a shortage economy it leads to further deprivation of the non-government consumers as the government is able to increase its share of consumption. The increased demand leads to a further increase in prices. In this case, people with a fixed income or those holding money reserves are the first to suffer as the fixed amount of money in their hands come to represent less and less of goods in physical terms which they are able to buy and their incomes lag behind the movement of prices. Professionals, employees and workers are the main sections who have to carry the main burden in a runaway inflation. But the revolutionary government which had come to power on a promise to safeguard and promote social and economic interests of the working class could not, with any moral justification, conduct a deliberate policy of curtailing the already meagre income of the workers in real terms. Therefore, the government resorted to paying the workers in kind in exchange for the amount of work done by them. Though it did not stop the overall deterioration of their economic conditions it did to quite an extent cushion the adverse effect of inflation on

inflation. Firstly, it was the huge mass of the peasantry which had to buy industrial products from the urban market and, secondly, the moneyed class consisting of businessmen and professionals (private doctors, engineers etc.). The position of the peasants was unique in the sense that they had to doubly bear the burden. Firstly, a grain monopoly was introduced after the revolution in order to curb the rise in the prices of agricultural products. Therefore, with the inflation progressively getting out of control there was a steeper increase in the prices of industrial goods as there was no restraining factor unlike in the case of agricultural goods. So now the peasants in reality could get less of industrial goods in exchange for the same amount of produce. Secondly, there was always a longer lag of time between receipt of payments by the peasants and their consequent spending for purchase of industrial goods. In the meantime the amount of money held by them would fall in value in real terms due to extremely high rate of increase in prices of industrial goods.

Under these circumstances the peasantry reacted in the only way possible in order to minimise their losses. The peasantry resorted to dehoarding of money. It now kept as little of paper money with itself as possible and instead started holding stocks in physical form, that is to say, it started buying and hoarding industrial goods in larger quantities than it did previously and, secondly, parted with their produce only in as much as it was necessary at a given point of time. The peasantry also realised that it can minimise its losses by cutting the time interval between the sale of its produce and purchase of goods during which it held money in balance. These practices of the peasants led to a heightening of upward pressure on the market price of industrial products and naturally resulted in a new round of price increases with a subsequent fall in the value of the currency. The government was thus not very successful in its policy of acquiring large quantity of extra resources by printing more money. It is estimated that by 1920 the ability of the government to raise extra resources by printing excessive amount of money was drastically reduced and the value of resources it could raise thereby was only a third of the real value of the currency in 1918.

Check Your Progress 2

1) Describe the general conditions during the Civil War period.

.....
.....
.....
.....
.....
.....
.....
.....
.....
.....

2) State briefly why the government was forced to resort to the printing of the excessive amount of money.

.....
.....
.....
.....
.....
.....

10.4 WAR COMMUNISM AS AN ECONOMIC SYSTEM

The government was forced to take radical policy decisions especially relating to the

exchange between the various sectors of the economy and broad sections of the society.

10.4.1 Economic Measures of the Soviet Government

The market mechanism had proved its inadequacy for achieving the objectives of the government. A new system was needed and it was adopted as a series of urgent economic measures in relation to the peasantry and agricultural production. The government moved to take control over the distribution and supply of agricultural produce, even if it meant use of coercive methods. Now it would be the government which would decide how much of the agricultural produce will be left with the peasantry. In other words, what would be the quantity which will be requisitioned by the Government on an obligatory basis as surplus produce? Where and how much of the surplus thus acquired will be directed? Therefore, the cornerstone of this policy was centralised collection and distribution of agricultural surplus. The organisation of this system was handed over to 'Narcomprod' or the Ministry of Supplies.

Such a policy could only antagonise the peasantry as it went against its interest as an independent economic entity, which could, and did in certain region, bring about a rupture in the alliance of the workers and the peasantry against the previous regime. Apart from serious political consequences, pursuance of this policy, as historical events were to prove, was also fraught with very serious economic consequences. The peasant who was now not able to utilise the reward to his labour according to his own free will and was forced to part with a large part of it, retaining only that amount which the government thought would be sufficient for him, did not have motivation to work beyond a certain limit. As a result of this lack of motivation, the peasant, naturally, started to sow only a part of the land he had, a practice which on a nationwide scale led to a substantial shrinkage in the area sown. With substantial shrinkage of sown area in a short period of time coupled with primitive methods, agricultural production had the inevitable result of going down. The total crop yield by 1920 had declined by more than a third.

This was also a period of extensive nationalisation of industry. Nationalisation was then not restricted only to enterprises of crucial import for the government, but all the large scale and medium as well as a majority of small and very small scale production units were nationalised because of the complications of coordinating the centralised distribution of agricultural and industrial resources and consumer goods among the rural population, industrial workers, industrial enterprises, the army and other government agencies. A decree was issued on November 1920 regarding the kind of enterprises to be nationalised. According to the Decree all production units where mechanical power is used and more than five people are employed, and those where mechanical power is not used with more than ten people employed were to be nationalised. Such a massive nationalisation led to 37 thousand enterprises being transferred to the jurisdiction of the State, among which there were thousands of small factories both using and not using mechanical power.

During this period (1918-1920) the government came to monopolise and control the movement of all the productive inputs as well as commodities meant for individual consumption. Most of the distribution activities were now conducted in kind, the market mechanisms were almost eliminated which led to exclusion of money as a viable medium of exchange. The exclusion of money as a medium of exchange was facilitated by two Decrees of 1918—one of which made it obligatory to carry out exchange only by means of book entries, and the other prohibited all internal trade and the function of supplying goods for individual consumption was given to Narcomprod.

It was necessary for the government to identify and elaborate a system of well defined transactions between its agencies involved in the organisation and control of the distribution process on the one hand, and the producers, be it the peasant or the worker, on the other hand. As far as the workers were concerned such transactions were rather simple—they were paid an equivalent of the work performed by them in kind. But such transactions were rather complex to organise in the case of equitable exchange with the peasants in view of determining the relative value of the commodities involved and the minimum amount to be left with the peasant. The government therefore proceeded to divide the whole range of agricultural products

type of product. The agricultural products were thus divided into three categories :
i) products which were to be requisitioned on an obligatory basis; ii) those which were not to be requisitioned but could be sold only by government agencies, and iii) those products which could be freely traded or exchanged in kind. Here again the results were not exactly in line with the expectations of the government. It had expected to increase the availability for itself of those products which were of importance for the government by means of compulsory requisitioning. But the peasants again were least motivated in the production of these products. On the contrary they were interested in growing or producing products included in the third category.

10.4.2 Centralisation

The government reaction to such practices of the peasants was to transfer more and more products from the third category to the first. Apart from this the government made provisions for giving certain incentives to the peasants so as to persuade them to put additional stocks at the disposal of the government. These additional collection to some extent could supplement the stocks procured through compulsory requisitioning. The procedure used involved organising a special fund of industrial goods which was then put up for sale in the peasant market. At the initial stages sale and purchase was conducted by medium of money. But the Decree of 1918 announced that industrial goods would be supplied only against receipts of grain delivery. Hence, such transactions began to be conducted without involving money transfers giving rise to a system of barter trading between different sectors of the economy.

A large number of government agencies and cooperatives were included in the system of control. The apex bodies in the structure of this system were 'Narcomzem' or the Ministry of Agriculture and Narcomprod mentioned earlier. These were the agencies given the responsibility for collection of goods included in the first category. Consumer cooperatives as well as agricultural cooperatives were used in order to carry out the task of distribution of the industrial goods to the rural population and the agricultural produce to the industry in the form of foodstuffs and raw materials according to the plan chalked out by 'Narcomprod'. Involvement of a large number of agencies in the distribution process necessitated a proper classification of the transaction according to the criteria of category of goods in order to identify the role and functions of these agencies. If the cooperatives were to be involved in the distribution of the products included in the first category they needed to procure special licences for the purpose and were obliged to carry out the plans of the State. Secondly they could act as independent trading agencies and take part in the distribution of products in the other two categories. In carrying out the orders of the State the cooperatives simply passed on the industrial goods fund to the villages, exchange it for the peasants' produce and deliver it to the State. Needless to say, with an increase in the number of goods being transferred to the first category from the other two, the scale of independent functioning of the cooperatives was proportionately reduced. This centralisation of decision making was not in the least to the liking of the cooperatives as they had until then acted as independent economic entities and were used to taking independent decisions regarding their priorities. Now they were reduced to a position of subordinate agencies of the Government. A brief tussle ensued between the 'Centrosoyuz', a kind of super union of cooperatives, and the government, but in the end the government managed to gain control of this super body of the cooperatives with the help of industrial cooperatives where the bolsheviks were in a majority. This brought about a very high degree of centralisation of the distributive system.

If the compulsions of the civil war in Russia forced the government to take specific measures and counter measures which finally led to an extreme degree of centralisation of the distributive and supply system, then these very compulsions were also a cause of a similar process of centralisation of industrial administration.

Immediately after the October Revolution the bolsheviks as we had seen had conducted nationalisation on a limited scale due to many factors. They had also tried to create new organisational forms. They had also been quite successful in establishing two different kind of organisations suitable for the purposes of administration of industrial production both in the light and heavy industrial sectors - 'centres' for the

forms in themselves had promoted centralisation of industrial administration, albeit on a very limited scale. But, later, deteriorating economic conditions and setbacks at the various fronts forced the bolsheviks to accelerate the nationalisation of the industries and rapidly expand it to include almost whole sectors and a major part of the industrial sector in general. All of these nationalised industries were now being turned over to 'glavkis' and 'centres' with a parallel increase in the number of such organisations, especially of the latter, as this form provided the government wider opportunity to control the administration of the enterprises under the 'glavki'. But with further deterioration of the situation and the imperative of dovetailing and coordinating the work of the enterprises with the working of a centralised system of distribution, the government which had earlier been conducting only the function of general co-ordination, very soon was forced to concentrate in its hands the task of controlling even the operative work of the units under various 'glavki'. When the number of enterprises increased substantially and they came to be concentrated in a fairly large number of 'glavki' (about 50 in 1920) which were in turn subordinated to the Vesenkha, it became impossible for the Vesenkha to co-ordinate their operations. So a **Utilisation Council (UC)** was formed as an apex body and was subordinated to the Vesenkha. Thus we see that in industry too the decision making came to be concentrated in a single centre - UC of Vesenkha, just as agricultural dealings came to be concentrated in Narecomprod.

Overcentralisation of the economic system inevitably resulted in hypertrophy of the State's Administration system. The staff in the administrative sections was increased manifold and a new Soviet bureaucracy was created which far from solving the problems was now interested in only 'paperwork'. As a result crucial decisions were not taken in time. And when taken they were often not implemented fully and in time or implemented only on paper as again what concerned the bureaucracy most was the report on its achievements and not implementation in reality. The bureaucrats in the Central bodies would not know the conditions of places situated far from them. Yet they made decisions regarding the vital interests of the people living there about which again they had inadequate information. The result was that most of the time they could not take timely and proper decisions.

Massive disruption of the economic linkages and discontent among the people specially the peasantry which was most severely affected was the result of these policies and became a real threat for the Soviet government. A series of revolts broke out and it was these revolts which convinced the government about the undesirability of continuing these policies. New economic policy was thus made an historical imperative.

Check Your Progress 3

1) **Into what categories were the agricultural products divided?**

.....
.....
.....

2) **What were the ill-effects of requisitioning?**

.....
.....
.....
.....
.....

3) **Explain the phenomenon of centralisation.**

.....
.....

10.5 LET US SUM UP

The crux of the economic system of War Communism was the policy of requisitioning. Nationalisation was the second major policy of the system of War Communism. Private trade was reduced to the minimum. These were the most salient features of War Communism. The government was cut off from most of its supply sources of almost all the material inputs needed for the armament industry as well as of supplies of foodstuff. It resulted in near starvation conditions in the towns. The government had to take radical steps in response to such a crisis. This response took the form of nationalisation of large sectors of industry, abolishing of private trade centralisation of the distribution system.

These forced economic measures allowed the Soviet government to collect enough resources for winning the Civil War, but clearly brought in their wake economic disruption and social discontent on such a scale that the government was forced to discontinue many of these practices and adopt a new economic policy.

10.6 KEY WORDS

Glavki : An organisation by which the Soviet government controlled the production process in the various sectors of the heavy industry.

Narcomprod : Ministry of Supplies dealing with the policy of centralised collection and distribution of agricultural surplus.

Requisitioning : Compulsory confiscation of a part of the peasants' produce above the amount needed for his subsistence and sowing for a payment in money or kind.

Syndicalism : Factories run by workers primarily for their own benefit.

Vesenkha : Supreme Economic Council, the apex body for all 'glavki'.

10.7 SOME USEFUL BOOKS

Nove, Alec, 1969, *An Economic History of the USSR*, Ch. 2-3, London.

Carr, E.H. and R.W. Davies, 1969, *Foundation of a Planned Economy*, Vol-1, London.

Szamuely L., 1974, *First Models of the Socialist Economic Systems*, Budapest.

Dobb, Maurice, 1960, *Soviet Economic Development Since 1917*, 5th ed., London.

10.8 ANSWERS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) Read section 10.2.1 to answer
- 2) (a), (b) and (d), are false
- 3) Read 10.2.2 to answer
- 4) (a) and (b) are false. (c) is true
- 5) Read 10.2.3 to answer
- 6) Read 10.2.3 to answer

Check Your Progress 2

- 1) Read 10.3.1 to answer
- 2) Read 10.3.2 to answer

Check Your Progress 3

- 1) Read 10.4.1 to answer
- 2) Read 10.4.1 to answer
- 3) Read 10.4.2 to answer



ignou
THE PEOPLE'S
UNIVERSITY

UNIT 11 SOVIET ECONOMIC DEVELOPMENT : 1921-1928

Structure

- 11.0 Objectives
- 11.1 Introduction
- 11.2 Background
- 11.3 The New Economic Policy
 - 11.3.1 The New Policies
 - 11.3.2 The "Scissors" Crisis
- 11.4 The Industrialisation Debate
 - 11.4.1 The Marxist Paradigm
 - 11.4.2 The Debate
- 11.5 Let Us Sum Up
- 11.6 Key Words
- 11.7 Some Useful Books
- 11.8 Answers to Check Your Progress Exercises

11.0 OBJECTIVES

After reading this unit you will know about:

- the most salient features of the new economic policy initiated by the Soviet Government after the Civil War was over;
- the problems that arose when the NEP was implemented, especially the scissors crisis; and
- the debate on industrialisation of the country.

11.1 INTRODUCTION

The economics of War Communism had brought about in its wake large scale disruption of linkages between different sectors of the economy, maladministration and serious bottlenecks in the supplies of foodstuff and raw materials. It was realised that such a situation cannot be prolonged without serious repercussions for the Soviet regime. The discontent was now not limited only to the villages but had also spread to the towns and was gaining ground in the army. The revolt against the government in Kronstadt near Leningrad by the sailors of the Baltic Fleet, which had been the bulwark of the October Revolution, convinced the Soviets that any delay on this issue was impermissible. The industrial production in all parts of the country was completely paralysed.

11.2 BACKGROUND

The crux of the crisis situation lay in the relations between the workers and the peasants, between the countryside and the urban centres. During the period of War Communism, the alliance of the workers with the poor and the middle (or well-to-do) peasantry came under severe strain and was on the brink of being broken irreversibly. Lenin, who had championed the cause of such an alliance was greatly disturbed by the developments and was among the first in the leadership to realise that if no attempts were made urgently to restore the worker-peasant alliance, it would be impossible for the revolutionary regime to survive. It was realised that if the revolutionary proletariat wanted to win back the peasants as their allies in their struggle they would have to take immediate economic measures. These measures would not only take full account of the peasants' interests but would further promote these interests as an integral part of the economic policy, thereby restoring the confidence and goodwill of the peasantry

towards the revolutionary regime.

But, at this point of time, there was a deep **division within the ruling Bolshevik Party**, though not specifically on the issue of the relations with the peasantry. The divisions in the party were facilitated by the fact that it still did not have adequate time to assess the policies of the War Communism period. It was recognised by all that there were serious shortcomings in the economic policies of War Communism. But it was still not clear which policy or set of policies had a negative impact and which policies had proved to be beneficial on the whole. It was still not clear to everybody where exactly lay the weakness of War Communism as an economic system, which weaknesses were incidental and which among these were inherent in the system. Therefore, it was even more difficult for the Soviets to formulate any clear cut economic policies which would substitute War Communism or extent to which such substitution was really a necessity.

Paradoxically, it was the centralisation of the production process which became the first object of attack by those who wanted a change in the economic policies of the government. This attack came in the form of a strong demand for curtailing the power of the 'glavki' which had become all pervading during the Civil War. It was demanded that industries which were not of crucial and national importance should be excluded from any kind of interference from the 'glavki' and subsequently be handed over to the 'provincial' (local or district) economic councils. Thus, excluding just a small number of industrial sectors, the rest were transferred to the jurisdiction of the districts and their economic agencies. Consequently, a substantial decrease in the number of the 'glavki' was also effected - from 52 to 16.

Naturally, this measure did not solve the basic problem, which consisted in the inability of the government in substituting the market mechanism by an equally efficient mechanism regulating the economic activity in the country. This fact was clearly recognised by the government. The question of real autonomy of industrial enterprises became a contentious issue in the party as centralisation is integrally linked with the role of the workers and their rights (as well as that of their organisations - the Trade Unions) in controlling the process of production and the allocation of the products of their labour. The debate on these questions took the form of a discussion on the relationship between the State and the Trade Unions, on their role in managing the production process in their respective enterprises - a discussion which brought about sharp divisions in the party.

The debate on the role of the Trade Unions in the management of the economy at first glance may not appear to have any relevance to the formulation of an alternate economic course of the economy. But the divergence of views that were expressed by various factions of the party on matters of principle showed a clear **split in the party** along various ideological lines. This split was to have far reaching consequences for further developments - economic as well as social and political - in the country right up to the final victory of Stalin.

The radical group was represented by Trotsky who wanted labour to be organised along military lines by organising trade unions. These would be transformed into brigades of a labour army with its officers appointed by the government. This line of action called for what is now known as '**statisation**' of the Trade Unions which would make them subordinate departments of the State. There was another group known as the '**buffer group**' which included Bukharin and Zinoviev. This group wanted a compromise between the official line and the '**statisation**' line of the Trotsky group. It later split into two, one part joining Lenin and the other Trotsky. The other line, which was to become the official one, in the party was represented by Lenin and some other prominent members of the party including such important veterans of the Bolshevik Party as Kamenev, and Zinoviev. Stalin too had supported this group. There were some other minor groups also like that of Ossinsky (who was to play an important role later during industrialisation debate). It was, finally, the Lenin group which prevailed in the party. The basic principles which were advocated by them included i) that the trade unions must retain independent position; ii) they must take upon themselves the responsibility of defending workers' rights and iii) that they should also be responsible for maintaining discipline and promoting labour productivity at the work places.

It was at this point that it was realised that the problem of the role of the workers and their trade unions was not such a major problem, and that there were matters much more serious which demanded urgent and immediate attention and the most urgent

being a new policy in relation to the peasantry with the main purpose of restoring and strengthening the 'smychka' or the alliance between the workers and the peasants.

11.3 THE NEW ECONOMIC POLICY

The new policy formulated by the Soviet government as an alternative course for the country's economy, replacing the War Communism system of hypercentralisation and all pervading bureaucratic controls and other administrative excesses, was a forced one. The Soviet government was under extreme pressure to give the peasantry wide ranging concessions. It must be stated that the Soviet government and the Bolshevik Party considered the concessions made during the NEP to be of a temporary nature.

At this point of time there was no alternative to the reintroduction of the market mechanism into the functioning of the economy, while at the same time striving to combine it with a certain degree of state regulation. Most of the sectors of crucial import for the functioning of the economy — the basic industries, foreign trade, finance, transportation and banking — were now retained in the hands of the state. This constituted a much larger portion of the economy than that which came under state control during the first eight months of the Revolution. However, this was significantly less than that which was forcibly put under direct and strict state control during War Communism. Most of the largest and the medium enterprises, encompassing approximately three quarters of the industrial production, thus still remained under government control. All of the other enterprises were denationalised which were now allowed to make their decisions. In this manner agriculture was now again put in the hands of individual farmers and a large portion of the industry in the hands of individual managements. These measures led to restoration of market links between industry, agriculture and the consumer and to a proportionate decrease in state control over production and distribution. It was thought that organisation of the economy along these lines now make it possible for the government to provide general guidance to the economy through exercise of control of the crucial sectors. Simultaneously, ample space for the operation of market forces would lead to efficiency and higher productivity of the economy through the functioning of the denationalised sector.

The objective of the NEP was not simply to provide incentives to the economic players to produce better results in terms of increased output and productivity. It had also a major political objective which, perhaps, taking the overall situation into consideration, was of more importance for the Soviet leadership than the purely economic aspect. Perhaps, the political aspect of NEP — the alliance ('smychka') — was considered of prime importance by the leadership as it saw the restoration of this alliance to be the crux of the existing difficulties. The alliance with the peasants could be effectively restored only if the Soviets gave the former some respite from the rigidities of the system of requisitioning. It was thus clear that the degree to which the peasant would now support the Soviet government would depend on how far the government was prepared to go in the direction of 'freeing' the peasant from the clutches of War Communism. Specifically requisitioning and reestablishing market agriculture would allow the peasant to both sell and buy according to his own individual needs. The Soviets in this case took the most radical measure of completely abolishing the policy of requisitioning and replacing it with a tax on net income, first in kind and later in money.

This politico-economic strategy now dictated its own logic to the Bolsheviks. First of all, it acted as a constraining factor for the Soviet government. It was restricted to only those policies which would not alienate the peasantry. This was not easy for the Soviets as the consequences of 'smychka' were not always in concordance with the ideological objectives of the Bolsheviks. For example, the marketisation of agriculture inevitably led to the creation of a prosperous class of farmers, and thus to greater economic differentiation in the villages, a situation certainly contradicting the egalitarian underpinning of the Communist ideology.

11.3.1 The New Policies

As, has been mentioned earlier, the cornerstone of the New Economic Policy adopted by the Soviets to replace the economic system of War Communism was the

Introduction of a proportional agricultural tax on the peasant – the ‘prodnalog’ – in place of the compulsory requisitioning of the peasants surplus produce. The State now took only a fixed proportion of the peasants’ surplus or net produce, while the peasant being allowed to sell the rest of the surplus. Further, a provision was made for differentiation of the prodnalog according to income level and size of the family/household. The amount of the prodnalog varied from the minimum of 5 per cent of the annual income for those holding less than a quarter of a hectare to 17 per cent of the annual income for those holding more than three hectares. The overall quantum of the prodnalog was equal to half of the amount collected through requisitioning and was calculated on the basis of the minimum requirements of the army and of the workers employed in the crucial sectors of industry. As the State now acquired only a portion of the surplus the peasant was now interested in increasing its total output so that a larger amount is left with him to be used according to his individual needs.

It can be argued that there was very little difference between the requisitioning policy and the *prodnalog* of NEP. Instead of acquiring all the surplus as previously, now the government was taking only a part of it. It may seem to you that the difference now was only one of magnitude; that there was no qualitative difference. On a closer examination of the consequences of this policy any such assertion could be considered to be only partly correct for the following reasons.

Firstly, the peasant could now sell as much of the surplus left with him after the payment of the prodnalog; he could also choose the customer. In other words this measure led to the legalisation of private trade and putting it on an equal basis with trade in the government sector. This freedom on the part of the peasant meant **reintroduction of market** links between different sectors of the economy and that, henceforth, market mechanisms were going to determine the nature and magnitude of the development of a large portion of the economy.

Secondly, it also meant greater role of **money as the medium of exchange**. The reestablishment of the market on a fairly large scale inevitably led to a curtailment of the sphere of centralised distribution system.

The peasants’ right to freely trade its after prodnalog surplus was restored. This resulted in the abolition of the trade monopoly exercised during the War Communism period by the Narcomprod which was responsible for the collection and distribution of all of the surplus agricultural produce through a system of allocations to different consumers. One of the fallout of this step was that the cooperatives now regained their autonomous status as commercial agencies and were freed of the controls imposed on them by Narcomprod. The centralised system of food and raw material delivery and supply, which was organised by the network of the *glavkis*, was now terminated. It was replaced by a system whereby the industrial enterprises were supposed to make their own arrangements for acquiring raw materials and marketing of their products through independent contracts with other industrial enterprises or agricultural producers. A large portion of the industrial enterprises were now free to market their products proportionally to the amount of the raw materials they acquired through individual contracts. It resulted in decrease in central allocation of these materials to them.

There were two stages in the process of restoration of autonomy to the industrial enterprises. At first, they could market only half of their products and were obliged to hand over the other half of their output to the central authorities in exchange for raw materials, fuel and other inputs. Later the enterprises were given complete freedom in buying raw materials and fuel for their productive needs and selling their products in the market instead of dealing with the central agencies.

The economic measures promulgated as part of the NEP brought about significant changes, not only in the agricultural sector and the distribution system, but also in the industrial sector and its organisational forms. Apart from the fact that **industrial enterprises were now autonomous commercially, a large number of them were also denationalised**. Small production units employing up to twenty persons were denationalised and some of them were even restored to their former owners, while not a small number were leased out to private businessmen. This led to recreation of a new class of private entrepreneurs and small scale capitalists. At the same time it must be remembered that denationalisation was limited only to small scale industry comprising about thirteen per cent of the total industrial work force of the country, the rest being employed in the nationalised sector. Only two per cent of the output of large scale enterprises was produced in the private sector.

The large scale industrial enterprises, by and large, remained in the nationalised sector. However, they were now granted a much greater degree of independence in the decision making process which resulted in decentralisation of the administrative functions. The nationalised industry was divided into two categories: i) those enterprises which received central allocation of raw material and fuel, and continued to be financed from the central budget. This category consisted of enterprises belonging to fuel, metallurgy, war industries, transportation, banking and foreign trade sectors; ii) the rest of the enterprises, which were now factually independent of any kind of control, were instructed to conduct their affairs on the basis of commercial feasibility and profit maximisation. They could now sell to the highest bidder and buy from the cheapest source.

The changes brought about in the status of the industrial enterprises and granting of decision making authority to the majority of the enterprises necessitated changes in their organisational forms. The forms of *glavki* and centres which were devised for the purposes of a highly centralised economic system were now rendered obsolete and were unable to satisfy the requirements of the new economic system. Hence the need was felt for new forms of organisation of industrial enterprises. The enterprises belonging to the second category were now organised into **trusts**, which were granted legal authority to negotiate contracts independently and subjected to a very loose supervision by the government agencies. The latter could not legally acquire the property of the trusts except by mutual consent in the form of contractual agreement. The government exercised very little control over the trusts in the light industry, usually using the methods of monetary and fiscal intervention. It is estimated that by 1923 about 480 trusts were formed which accounted for about seventy five per cent of the work force engaged in the nationalised sector of the industry. Property and income tax were imposed on the trusts and private enterprises on an equal basis. In enterprises belonging to the second category the supervision of the production process was much more strict. These enterprises were subject to obligatory production and delivery targets. But the enterprises of both the categories were under instructions to conduct their affairs on the basis of profit generation and a subsequent minimisation of dependence on state subsidies. Cost accounting was asked to be effectively introduced in the operation of all the enterprises irrespective of the category to which they belonged. The trust, therefore, differed from the *glavki* and the centre in that they could not bind any third party except by contractual agreement. They were not State bodies but economic entities, and possessed only those powers which they could secure through contract. The trusts differed from a private company or even a joint stock company in that they did not employ any private capital and hence could not make use of private investments.

The need to simplify control and co-ordination with the purpose of providing a more efficient guidance to the economy as a whole during the NEP led to the formation of large amalgamations of producing enterprises which came to be known as '**syndicates**'. Initially the need to amalgamate trusts into syndicates was felt for the purpose of coordinating the sales of the hundreds of industrial enterprises. Amalgamation was also preferred by the authorities because they facilitated organisation of large scale production. The syndicates were given wide ranging autonomy and could even enter direct contracts with foreign partners by passing the state foreign trade monopoly. They could even receive credits from various financial institutions within the country and in certain cases even from foreign sources. The growing tendency towards formation of more and more syndicates led to formation of powerful monopolies which, as further developments showed, was to prove quite disadvantageous for a smooth course of economic recovery.

Another positive development of this period was the reintroduction of money into the functioning of the economy. The War Communism saw a complete erosion of the functions of money as an effective medium of exchange and it was almost eliminated due to hyperinflation. Money transactions during this period were replaced by a system of barter trade and physical allocations. The introduction of the market mechanism now required reintroduction of an effective medium of exchange and, therefore, of money. All the enterprises were now asked to conduct their transactions through the medium of money. They were also encouraged to put their savings with their banks by the removal of various limitations on bank deposits and by safeguarding such savings from confiscation.

All this goes to show that inspite of controls and general supervision the economic system under NEP was not one of a command economy. The role of the planning bodies was restricted to providing control figures. These figures served as a guide for individual enterprises in making decisions regarding investments. As mentioned earlier, mandatory output figures were given only to a small number of enterprises. It was the Narcomfin (Ministry of Finance) which was the major governmental agency exercising control and regulation of the economy through the budget and credit system.

11.3.2 The "Scissors" Crisis

The Soviet government decided to introduce NEP as a means to effective economic recovery after the devastating Civil War. The system of War Communism that was dominant during the period of Civil War had helped the Soviets to overcome the difficulties of that period. In the same manner, the NEP was supposed to serve as the means of economic recovery in the post Civil War Period. The recovery of the economy during 1921-1928 was quite impressive and proved that NEP was a very important strategic success.

At the end of the Civil War in 1920 the economic activity was at a very low level. Production level and transportation activity was at a level which was about only one-fifth of the pre-war level. Fuel was also in extreme short supply and it threatened to paralyze the economic activity in the country. Agriculture was also in dire straits showing a production level of only sixty four per cent of the pre-war level, leading to extreme food shortages and as a result to undernourishment and exhaustion of the population and, what was more serious, of the work force.

Table 11.1: Production and trade indexes, USSR: 1913, 1920, 1928 (1913 = 100)

	Industry	Agriculture	Transport	Export	Import
1913	100	100	100	100	100
1920	20	64	22	0.1	2.1
1928	102	118	106	38	49

(Paul Gregory and R. Stuart, *Soviet Economic Structure and Performance*, 2nd ed. 1981. p. 52).

In 1928, when the First Five Year Plan was to be implemented, industry and transport were marginally above the 1913 level, while agriculture surpassed the pre-war level by twenty per cent points. However Foreign Trade remained significantly below the level of the year preceding the War, though when compared to the level at the end of the War Communism period, it showed remarkable recovery.

The recovery which started after 1920 was such that by 1923 the economy had reached a level which was one-third of the pre-war level. This recovery, however, was not even and showed especially marked difference between the rate of growth in agriculture and in industry. Industrial output grew slower than the agricultural output. Therefore, in 1923 a situation was created wherein the amount of agricultural products coming on the market was nearer to the 1913 level as compared to the flow of industrial products. This comparative shortage of industrial products put an upward pressure on the prices of industrial products. However, during 1923, the rise in prices of manufactured goods was much more than the ratio of availability of the products of these two sectors in the market, which was estimated to be about 70 per cent in favour of agricultural products. Though the flow of agriculture goods was only 70 per cent more than that of manufactured goods, the relative change in prices of the products of these two sectors was 3 to 1 in favour of industrial goods. The relative price movements of the industrial goods and agricultural products during the period of almost two years, from early 1922 to the end of 1923, when charted in the form of a graph look like an open pair of scissors as you can see in Fig. 11.1 below. This was the reason why the phenomenon was called the 'Scissors Crisis'.

The discussion at that time regarding the causes of the scissors crisis was first conducted in the context of general price rate. It was only slowly that economists came to view the Scissors Crisis independently of the general question of inflation and price rise and to look for specific causes of the Scissors Crisis. The factor mainly responsible for the widening of the gap between the price levels of industrial and agricultural goods was the

monopoly position of Industry in the national market.

As it was mentioned earlier syndicates were created as new forms of industrial organisation as an answer to the new requirements of NEP.

(Paul Gregory and Stuart R. op. cit. p. 53; Their source A.L. Vainshtein, TsEMY itsenobrazovanie SSSR V Vostanovitelny Period, Moscow, 1972.)

These syndicates came to concentrate to a large extent the supply of a whole range of industrial goods in their own hands. It must be pointed out, however, that the syndicates did not exercise complete monopoly over industrial products and faced competition from trusts which had remained outside the syndicates. But the syndicates did control large enough share of the industrial supplies enabling it to conduct monopoly practices, especially one of manipulating prices. On the other hand, agricultural supplies were highly decentralised, dispersed and deregulated inspite of some efforts taken to the contrary by the government. Thus the situation in 1923 was such that the Industry could now face the peasants on the national market as organised monopolist having a tight control over the supply of their products.

Under these circumstances, like any economic player, there was a very strong desire for the Industry to change the terms of trade in its favour, which could be done most conveniently by manipulating supplies, more precisely by restricting the sale of its products on the market. Under usual circumstances, holding back of stocks cannot be sustained as it leads to increase in inventories and accumulation of stock, but in the specific conditions of that period it did not put any undue pressure on industrial enterprises as it gave them the opportunity to replenish its stock helped the government's liberal credit policy.

The government reacted by initiating a **two-fold policy** to get the 'scissors' to close. Firstly, the government took measures to counter the monopoly practices of the industry by putting pressure on industry to reduce prices; secondly, it took initiatives to raise the prices of agricultural products and provide credits to grain purchasing agencies on more easy terms. The industry was brought under pressure in three ways:

- i) price ceiling was introduced in the form of maximum selling prices;
- ii) the flow of credits to industry was drastically curtailed, and
- iii) goods were imported and put on the market in order to undercut the monopoly prices. As a result, by the beginning of 1924 the 'scissors' began to close.

The complex issue of managing the 'scissors crisis' threw up different views in the Communist Party regarding the necessity and relative advantages of such basic questions of policy as stabilisation of the currency, role of credit, price ceiling etc. The differences on these issues were certainly not limited to the specific question of managing a crisis situation but, as further events were to show, were a manifestation of two fundamentally diverging conceptions of the transition to socialism.

Check Your Progress 1

1) What was the main issue on which the Bolshevik party was divided towards the end of the War Communism period?

.....

.....

.....

.....

.....

.....

2) State whether the following statements are true or false.

- a) NEP was expected to be a permanent feature of socialism.
- b) All the sectors of the economy were denationalised.
- c) Requisitioning was abolished.
- d) NEP was in full concordance with Communist ideology.

3) What was the essence of the New Economic Policy (NEP)?

.....
.....
.....
.....
.....
.....

4) Describe the changes in the industrial sector?

.....
.....
.....
.....
.....

5) State whether the following statements are true or false:

- a) NEP led to decentralisation of the distributive system
- b) Money was abolished during NEP
- c) New forms of organisation of enterprises were devised
- d) Syndicates were amalgamated into trusts

6) What was the main cause of the 'Scissors Crisis', and what was the government's response to it?

.....
.....
.....
.....
.....
.....

11.4 THE INDUSTRIALISATION DEBATE

Though the NEP period is considered to have come to a close in 1928 — on the eve of the First Five Year Plan — there was considerable debate in the country after the closing of the 'Scissors' in 1924 on the ways and means of starting a phase of maximum economic development in the country which would bring about a complete dominance of the socialist economic relations. It was natural that a debate of such fundamental nature would raise a multitude of questions concerning development strategy — such issues as that of balanced versus unbalanced growth, agricultural savings, scope and role of planning, taxation, inflation and unemployment. It was a remarkable aspect of this debate that it had anticipated any such discussions in the much more advanced and industrialised countries of West Europe and the USA.

11.4.1 The Marxist Paradigm

Marx had very little to say about the future Communist Society. Marx had maintained that Capitalism would inevitably evolve into a higher form of social system, just as the social system based on slavery evolved into a feudal social system, which in its turn evolved into the higher social system of Capitalism. This change, he argued, is brought about by the contradictions inherent in a particular social system independent of the will and desire of individuals. The inherent contradiction between wage labour and capital, between class of workers and the class of capitalist would necessarily lead to the establishment of a socialist system. Marx had also pointed out that the building of

future Communist society would occur in two phases. The first phase would be a period of transition which would have quite different characteristics and features depending on the specific conditions prevalent in a given country at the time of the overthrow of Capitalism. The inequities prevalent in different societies could be eliminated only in the second stage of Communism.

The transition period, however, would not be without inequities of its own, both economic and social, as it is not possible to do away with them at one stroke without first preparing a proper framework for such purpose. The basic inequity would be in the distribution of goods according to a person's ability to contribute to the production process. This meant that those who were capable of contributing more would get more in return, and those who, for any reason were not able to contribute to the extent of the former would get less. Though in this system there would still be inequality in satisfying the individual's needs it would be more fair in that it would provide more social justice and exclude exploitation. This system would form the basis of economic growth leading, eventually, to greater abundance of goods when it would become possible to distribute goods according to a person's needs. But Marx had not formulated any specific model of socialist economic growth. The model he described related to economic growth in a capitalist society and the necessary relationships between its two crucial sectors — Sector I, the sector producing means of production and Sector II, producing consumer goods. The conditions which would allow for economic growth or 'expanded reproduction' are different from that of a stationary economy or in Marxian terminology 'simple reproduction'. Expanded reproduction is possible if the output of Sector I exceeds the depreciation values of sectors I and II; and capital accumulation is equal to the difference between the output of Sector I and the depreciation values of I and II.

From this model we may derive a general idea regarding a blueprint of the future economic system of socialism, if at all one can make any meaningful prediction about future.

- i) distribution is according to contribution to production;
- ii) the essential relationships between sectors be maintained, preferably by some kind of planning;
- iii) priority be given to investment sector;
- iv) capital accumulation was based on expropriation, similarly, socialist accumulation can be conducted by expropriating the capitalists.

11.4.2 The Debate

The debate on the issue of industrialisation was dominantly about what kind of an economic system must be evolved; one that would be something like the NEP or something like War Communism. **The Balanced Growth Model** had Nikolai Bukharin, a leading Marxist theoretician and prominent veteran of the Bolshevik Party, as its main proponent. He was also closely related to the activities of the right wing of the Party after the NEP was introduced though he had earlier adhered to the left wing.

The proponents of the balanced growth model considered that it was not necessary to conduct discriminatory measures as a part of a deliberate policy in order to achieve industrial growth which would grow more rapidly than the rest of the economy even without such government action. Bukharin was convinced that the proletariat was strong enough politically to contain the capitalist tendencies of private agriculture. **The continuance of the market relations between different sectors** of the economy, more specifically between agriculture and industry, would not only be not disruptive, but would provide for a harmonious development of the relations between the peasant and the workers thus strengthening their alliance ('smychka'). A policy which would favour one sector over the others would only prove to be counter productive because of the **interdependence of the sectors** and the branches of the economy. Successful functioning of the industrial sector presupposes regular supplies of agricultural raw materials at more or less stable prices and supplies of foodstuff to the worker to make him physically fit for high productivity labour. Further, under conditions of acute capital deficiency which prevailed at the time, industrial growth was not possible without large quantities of imports from the industrialised countries of equipment and machinery in exchange for agricultural produce, as the sophisticated capital equipment could not be

immediately produced within the country. On the other hand capital investment in agriculture did not require such sophisticated and imported equipment. The indigenous industry could fully cope with the production of relatively simple tools and agricultural machinery required by the countryside. A shortage of such products of the industrial sector may force the peasants to once again resort to the practice of depriving the city of its products.

Bukharin favoured a gradual growth path for the economy with all the sectors expanding simultaneously. The basis of such growth would be the crucial links between the industry and agriculture which would be maintained by creating an atmosphere devoid of the uncertainties that had so far plagued the economy. Also a certain degree of incentives for the peasants initially would be provided, so that they were able to return to their traditional frugal way of living, thus creating the savings needed to finance the growth of industry. The industrial sector, in his opinion, should make the best use of the capacity available to it using it to the maximum by organising multiple shifts. The government on the other hand was required to pursue such a price policy which would promote cutting down of production costs and more efficient use of the resources.

Unbalanced Growth Models were proposed by two radically different groups one of them favouring discriminatory government policies in favour of industry and the other favouring agriculture as the priority area for investing relying mainly on the operation of the market forces.

The unbalanced growth of industry was favoured by the left-wing radical Preobrazhensky. He considered this model as the only alternative to a long term stagnation of the economy. He was convinced that half measures were not going to help and the only solution lay in a steep increase in investments in the industrial sector. In his analysis of the problems facing the country and the possible solution of these problems, Preobrazhensky proceeded from the premise that the main factors at the root of the economic difficulties were,

- low industrial capacity and,
- low propensity to save as the result of the change in the peasants' position in the society in the wake of the October Revolution.

He argued that the peasant was subjected to non-economic forms of pressure to save during the period preceding the Revolution as he was supposed to part with a part of his output to the landlord or the state. This forced surplus constituted savings in real 'terms'. As a result of this the buying capacity of the peasants was limited. The Revolution changed this arrangement by eliminating the rent payment and reducing agriculture tax to one-third of the pre-war level. This in its turn led to an increase in the peasants' demand for industrial goods while the industrial sector did not show any increase in its capacity.

The solution, according to Preobrazhensky, thus lay in **closing the gap between the peasants' demand for industrial products and the insufficient industrial capacity.** This would limit the industrial supplies by shifting the emphasis from consumption to saving, which could then be used for increasing industrial capacity. Preobrazhensky put special emphasis on giving **preference to the industrial sector over agriculture** in the development policies of the government. And even within the industrial sector heavy industry was singled out for most preferred treatment. This would enable the fledgling Soviet economy, in a long-term perspective, to greatly increase the production capacity. As a result the demand for consumer goods and agricultural machinery would be satisfied. He also realised that, in the meantime, the economy would be put under severe inflationary pressures. He sought to tackle this problem by his '**primitive socialist accumulation**', which would act as a counterbalance to the market setting the prices and would force and channelise the savings into capital investments. Primitive socialist accumulation would be used for the transfer of resources away from the private peasant economy to the socialist state sector on the basis of non-equivalent exchange between the agricultural goods and industrial products enforced by the state's pricing policy.

The supporters of the model of unbalanced industrial growth were certainly aware of the serious consequences of such a policy of deliberate and forced transfer of resources from private agriculture to industry. This was a lesson which they learned from the

experience of War Communism. Whenever the peasant is faced by rapidly deteriorating terms of trade they react by withdrawing from the market, and if force is applied they react by cutting down the area under cultivation and hence producing less. This tendency on the part of the private producers was ought to be countered by **increasing the share of state and collective farming.**

The **unbalanced growth of agriculture** on the basis of the market forces and not direct government intervention was favoured by the right wing of the Bolshevik Party. Lev Shanin was a prominent spokesman of this school of thought. Shanin like Preobrazhensky, also took serious note of the imbalance between the prices of the industrial and the agricultural sectors as well as of the accompanying inflationary pressures. However, unlike Preobrazhensky, Shanin pointed out that the problem of **income generation was the crucial factor** in economic growth under the circumstances existing at the time in the Soviet Union.

While arguing the case of **preferential treatment for the agricultural sector**, Shanin's logic followed a pattern which was rooted in two basic assumptions.

- (1) Shanin held the view that the marginal output capital ratio is substantially higher for agriculture than for industry. This meant that each unit of rouble invested in agriculture led to higher increment in output in the short-term.
- (2) Another feature emphasised by Shanin was that the industry was characterised by higher average and marginal propensity to consume, whereas the average propensity to consume for agriculture was high while its marginal propensity was low.

The inevitable conclusion which he drew from the second assumption was that if income distribution in terms of money is so organised that agriculture was favoured, it would lead to increased aggregate saving. The conclusion he drew from the first assumption was:- if a certain amount X is invested in agriculture and the same amount in industry, and the increase in the capacity of agriculture is 'a' and in industry 'b', then because of relatively larger marginal output-capital ratio of agriculture in comparison to that of industry, 'a' would be more than 'b' ($a > b$).

Investment in agriculture would also **exert deflationary pressures**. Increased investment in this sector would lead to increased income for the peasants. As the marginal propensity to save in agriculture was assumed to be higher in agriculture it would lead to comparatively higher aggregate saving, which would exert downward pressure on the prices of industrial goods. Higher investments in agriculture and the resulting increase in the agricultural production and availability of agricultural goods would also allow the country to gain benefits from foreign trade. Increased export of agricultural goods would create an opportunity for the country to import in exchange machinery and equipment which, given the prevailing conditions, could not be produced in the country, thereby promoting industrial development and at the same time neutralising inflationary pressures on the economy. Notwithstanding obvious benefits to be gained by the model of unbalanced growth of agriculture, there were some glaring weaknesses which in the final analysis proved to be the main reason for its rejection by the Soviet government. Shanin did not fully take into cognisance the fact that the possibility of foreign trade was extremely limited given the hostile attitude of the West towards Soviet Union; it did not take into account that some very considerable investments had to be made in sectors like transport and communications in order to build up an efficient economic system, thereby acting as constraining factors for large investments in agriculture; military requirements dictated the necessity of immediate enhancement of armament and metal industry.

Check Your Progress 2

- 1) What are some of the features of a Socialist system that we can derive from Marx's works?

.....

.....

.....

.....

.....

2) Briefly describe the salient features of the balanced growth model.

.....

.....

.....

.....

.....

.....

.....

.....

.....

3) Briefly describe the salient features of the unbalanced growth model.

.....

.....

.....

.....

.....

.....

.....

.....

.....

11.5 LET US SUM UP

The end of the Civil War saw the introduction of a new system of economic organisation and management based not on directives from the central authority but predominantly on the market forces and autonomous economic entities and private agriculture. Money was now reintroduced and became the main medium of transaction replacing the earlier system of book entries into the accounts of the enterprises of the amounts owed to or by them.

Though the economy now was well on its way to recovery and by 1923 had approximately reached the pre-war level, new problems had cropped up, eventually leading to a crisis situation — known as the Scissors Crisis — which threatened to disrupt the process of economic recovery and was reflected in a large gap between the prices of industrial and agricultural commodities and increasing inflation. The search for a possible solution of the existing problems led to a debate which very soon spilled over to a full fledged discussion about the fundamentals of economic growth and the means of it. This debate showed serious differences in the Bolshevik Party on all the issues concerned, differences which surpassed all earlier differences in the Party in the sharpness of tone and bitterness which accompanied them.

During this debate which has come to be known as the “Industrialisation Debate” three alternate models of growth were put forward by the three groups in the Bolshevik Party. The remarkable thing about this debate was that it had pre-empted any such debates in the developed countries of the west by about two decades and thus is considered to be a very original contribution of the Soviet economists to the theory of economic growth.

11.6 KEY WORDS

NEP: the New Economic Policy initiated by the Soviet government to replace the system of War Communism in 1921.

Primitive socialist accumulation: deliberate policy of transfer of resources from the private sector to the state sector in order to lay the foundations of a socialist economy.

Prodnalog: tax, initially in kind and later in money, levied on the net income of the peasants, which replaced the requisitioning system of the War Communism.

Scissors Crisis: steep increase of prices of industrial products in comparison to the rise of agricultural goods.

Syndicates: amalgamation of trusts formed during the NEP reform.

11.7 SOME USEFUL BOOKS

Nove, Alec., 1969, *An Economic History of the USSR*, London.

Carr, E.H. and R.W. Davies, 1969, *Foundations of a Planned Economy, Vol. 1, part 2*, London.

Dobb, Maurice, 1960, *Soviet Economic Development since 1917*, Cambridge.

Szamuely, L. 1974, *First Model Socialist Economy*, Budapest.

11.8 ANSWERS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) Read section 11.2 to answer
- 2) a) false
b) false
c) true
d) false
- 3) Read sub-section 11.3.1 to answer
- 4) Read sub-section 11.3.1 to answer
- 5) a) true
b) false
c) true
d) false
- 6) Read sub-section 11.3.2 to answer

Check Your Progress 2

- 1) Read sub-section 11.4.1 to answer
- 2) Read sub-section 11.4.2 to answer
- 3) Read sub-section 11.4.2 to answer

UNIT 12 SOVIET ECONOMIC DEVELOPMENT : 1928-1941

Structure

- 12.0 Objectives
- 12.1 Introduction
- 12.2 Background
- 12.3 Foundation of Economic Planning
 - 12.3.1 The Planning Controversy
 - 12.3.2 Structure of Planning
- 12.4 The Five Year Plans
 - 12.4.1 The First Five Year Plan
 - 12.4.2 The Second Five Year Plan
 - 12.4.3 The Third Five Year Plan
- 12.5 Let Us Sum Up
- 12.6 Key Words
- 12.7 Some Useful Books
- 12.8 Answers to Check Your Progress Exercises

12.0 OBJECTIVES

After reading this unit you will know about:

- the creation of an economic system which later came to be known as the command economy,
- the most salient features of the command economic system, and
- the achievements and failures in formulation and implementation of the first three Five Year Plans.

12.1 INTRODUCTION

The year 1925 saw the beginning of a new stage in the economic development of the USSR. So far the efforts of the government were directed solely towards expanding the production on the basis of the existing capacities. There were too little resources and expertise at the disposal of the government to allow it to embark on a more ambitious programme of economic development. But by the year 1925 the economy had sufficiently recovered from the chaos and destruction of the First World War and the subsequent Civil war. Hence, the government, after assessing the pace and the level of overall economic growth, could now think not only of attending to the most immediate economic tasks but also about the more important long-term economic goals and the means of achieving these goals. The industrialisation debate seems to have been a fairly accurate reflection of this view in the Communist Party and the government.

The Communist Party and the Soviet government were now thinking in terms of new investments and new construction. The industrial production had already reached the pre-war level and the agricultural production was almost at the pre-war level. Therefore, the problem now consisted in drawing up a correct picture of the direction in which to proceed further, and of the means and methods to be used. As we have seen, there were wide differences in the Communist Party and the government regarding these issues. But a decision had to be taken sooner rather than later, as to which course among the ones propagated by the different groups would be best for the country. The decision that was finally taken was in favour of the model proposed by the left-wing of the party—the model of unbalanced industrial growth. Paradoxically, it was not the leaders of this group who decided the fate of the country by opting for this model of economic growth but those who had most vociferously opposed them during the preceding discussion.

12.2 BACKGROUND

In 1925, it became increasingly clear that, apart from the general backwardness of agriculture, there was one very important factor which had now become the major constraint in the development of the economy. On a close examination of the situation in the agrarian sector after 1925, it soon became clear that one of the main problems to have manifested itself during the whole period was that the **share of the marketed surplus of the peasant produce was lagging considerably behind the pre-war level**, in spite of the fact that both the gross agriculture production and the overall sown area had reached the pre-war level. In 1926, only 13 per cent of the grain production was being put on the market, whereas the same indicator for the last pre-war year was 26 per cent. This shrinkage of the amount of grain being put on the market led to lower urban consumption and, what was even more serious, to a very low level of export of grain and other goods. This considerably restricted the government's ability to import the much needed machinery and capital equipment for the industrial sector in exchange for agricultural products.

One of the measures which the government devised to tackle this problem was to effect some kind of price stabilisation of industrial products. The government once again attempted to coordinate the activities of the various grain collecting agencies, both government and non-government, by setting up the maximum and minimum price limits. As a result of this policy, the rise in the wholesale prices of the agricultural products, in the following year, was restricted to only 2 per cent. This success of the government in stabilising the prices, however, was not without negative consequences, as it gave rise to serious setbacks in production and in grain deliveries. This was bound to affect the consumption in the towns as well as the exports. Apart from the marketed surplus of agricultural goods obviously important for the towns as a source of foodstuff and for the export sector, its relevance for regions of specialised commercial farming was no less. Shortage of foodgrains, thus, not only affected production in non-agriculture sectors but also undermined efficient functioning of the most progressive section of the agrarian sector itself.

The situation, hence, was quite complicated for the Soviets because of the obvious dilemma of transforming the industry into a modern sector, thus providing the base for the development of the rest of the economy. At the same time it altered the age old character of Russian agriculture without seriously affecting the grain production and subsequent supplies of agriculture goods. The Soviet government, rightly or wrongly, found the solution to this dilemma in large scale cooperative farming.

It should be remembered that the cooperative movement was always given high priority by the Soviet government in its policies. But so far cooperation was restricted to the sphere of trading and credits. Now the government wanted to expand the sphere of cooperatives to the production sector also. But this task presented absolutely new problems for the policy maker, the type that had no precedents in the history of various reforms of the agrarian sector in Russia.

So far cooperation in the agrarian sector in Russia had evolved three types of organisational forms: (a) a very elementary form known as the **society for joint cultivation**. The peasants worked the land together and shared the yield according to the size of the households, but each of them continued to be the owner of his separate plot of land, implements as well as draught animals; (b) the so called **communes** in which the peasants members not only conducted collective farming but even organised their lives along communist lines; (c) the **artel** system in which the member peasants conducted their farming and shared the yield from the agricultural land which was now held in common with commonly owned implements, while their houses and house gardens continued to belong to each member separately.

The Soviet government, while looking for the most suitable form of cooperation to begin their drive for the collectivisation of the agrarian sector, came to the conclusion that the form of the 'artel' was most suitable as the preceding point. The logic underlying this decision of the Soviet government was that, while the 'artel' form contained all the progressive elements in the traditional mode of farming, it also provided a real opportunity to organise large scale agricultural production and other

activities on the basis of the use of modern mechanised methods. It was also expected that the organisation of large scale farming along the 'artel' lines would enable the government to procure a larger portion of the agricultural surplus for the market.

The results of organising farming activities along new lines, however, showed that the government was too optimistic in their assessment of opportunities for solving the problem of a steep rise in the efficiency of the farming sector provided by the new form of production organisation in agriculture. Although, there was a rise in the immediate future in the amount of grain finding its way into the market, there was no significant rise in the yield per unit of the area sown. Thus the expectations of the government were only partly fulfilled. The new policy of the government only served to save labour, but could not prove itself sufficient for solving the difficulty of providing an expanding economy — most notably an expanding industry and increasing population — with adequate stocks of raw material and foodstuff in the short-term. As the experiment proceeded, it became clear that it could only be achieved in the long-term or, in the most unlikely case of the most optimistic scenario becoming a reality, only in the middle term. It became more and more clear that the government could not possibly depend on the cooperation movement alone for even the short-term goals of procuring large increases in the marketed surplus of grains and cutting down the gap in the grain supplies.

This difficulty was now intended to be overcome by the government by introducing a set of administrative measures and simultaneously by a more far reaching policy of setting up state owned large scale farms — 'sovkhosi'. The government wanted to treble the area under the sovkhosi in the very near future so that they would be able to produce about one and a half million tons of grain. To help the sovkhosi in their functioning a special trust — 'zernotrest' — was formed. These measures did produce good enough results in order to convince the government about the feasibility of expansion of this form of the 'socialised sector' in agriculture. But any such expansion of the sphere of the state farms entailed extremely large amounts of capital investments, especially in the industrial sector producing equipment for the farming sector for the production of tractors, iron ploughs, harvester combines etc.

This policy of setting up artels in the cooperative sector and, additionally, of state farms was in order to primarily solve the short-term goals of increasing the marketed surplus. It had very far reaching consequences for the development of agriculture in the country over a long period of about fifty years. It proved to be both the source of strength as well as weaknesses which were to plague the agriculture in the future. The policy of the government, of promoting the 'socialised sector' in the economy as part of a deliberate policy by providing it incentives and concessions, created social antagonisms in the village between those ordinary peasants and the upper layer of richer peasants who came to view the new policies of the government as a threat to their profit making prospects. The prospects of competition and, what is even more significant of out surviving the socialised sector with all its advantages of preferential treatment in credits, farm equipment and, and sales, when the socialised sector could procure inputs for a guarantee of future supplies of grain to the government, were indeed too daunting for, kulaks. The only recourse that this richer stratum of the peasants now had was either sooner or later, to join the socialised sector or to organise some kind of an opposition to these new policies to stop them from being implemented by the government.

The new social unrest that was unleashed in the country resulted, eventually, in a headlong clash between the very rich, peasants or the 'kulaks', on the one side and the government and the mass of the 'bedniak' (the poor and the landless peasants), on the other side. Its political fallout had extremely negative and long-term effects not only for the agrarian sector but also for the social fabric, the political set up and economic development in the country. At first, the government was cautious in its treatment of the kulaks, but with the passage of time it initiated a policy of expropriating the kulaks as a class. This policy was used in the inter-party struggle and was finally to become a tool in getting rid of wide sections of the party members.

Check Your Progress 1

- 1) What was the major problem in U.S.S.R. agriculture on the eve of the First Five Year Plan?

.....
.....
.....
.....
.....
.....
2) What was the essence of the agriculture policy of the government in this period?
.....
.....
.....
.....
.....
.....
.....
.....

12.3 FOUNDATION OF ECONOMIC PLANNING

As we have seen, the problems that the Soviet government was faced with had a very unique feature of being under the compulsions of an accelerated economic growth without any real possibility of getting from abroad the considerable amount of resources which could not be generated in the short-term. The market mechanism as the events during the period 1921-1928 showed was not capable of providing the basis for this type of economic growth. The centralised methods of coordination of the productive and distributive activities proved to be inadequate as well. The developments of this period, especially in the Communist Party which witnessed the ascendancy of Stalin to the top of the leadership ladder, put the group which propagated the pre-dominance of planning in influential decision making process and relegated the supporters of the market to a secondary place. The industrialisation debate and the cooperative movement strengthened the hands of these elements, and the question now was no longer that of the market or planning but one of overall planning with some small sectors being allowed to operate in a market environment. Even these small islands of market economy were to be gradually integrated into the larger planned socialised sector.

It is, therefore, necessary now to turn the focus of our attention to the various aspects of the planning process — towards the methods of planning as well as the structure of the planning apparatus. The twenties of this century in the Soviet Union was a period of intense debate on the issues of

- the relevance of the alternate growth models,
- the relevance of planning and market,
- the type and scope of (socio-?) economic planning,
- advantages and shortcoming of the various alternate planning theories etc.

This discussion, which can be termed as **the planning debate** on analogy of the earlier industrialisation debate, was characterised not only by a bitter struggle of this or that group for recognition of their ideas as truly necessary or as the only truth, but also between various planning bodies and other government agencies for supremacy or at least a dominant position in the structure and hierarchy of the planning apparatus.

12.3.1 The Planning Controversy

During the period of the NEP, market relations were reintroduced on a large scale replacing the centralised system of planned distribution. It witnessed the origin of the debate on planning concerning itself with issues as different, though organically interconnected, as

- the role of planning in the country's development in the social and economic spheres,
- the scope,
- the kind of planning,
- its compatibility or its incompatibility with the operation of market forces.

This last issue in fact dominated the discussions forming the central theme around which the discussions regarding the merits and demerits of other aspects of planning were conducted. This issue of market versus planning was essentially a question of whether the market forces were going to provide the limits and the essential framework for the planners in the process of formulation of the plan, i.e., was it precisely the major task of economic planning to overcome the constraints limiting the choices of the economic players.

The planning debate showed that, eventually, the discussions came down to a struggle between basically **two groups**, notwithstanding certain differences on matters of detail within the members of each of the groups. One of the groups which included such eminent Russian economists of the time as N.D. Kondratiev (of the business cycle fame) and the Gosplan economist, V.G. Groman, argued for a demand directed economic planning and came to be known as the school of **economic geneticists**.

The economic geneticists greatly emphasised the significance of the role of the consumer demand in any policy making process as it is one of the most reliable indicators of the direction of the change taking place or about to take place. Hence, it would serve the planner as a viable tool in his search for proper orientation targets of the changes he seeks through planning. The geneticists viewed the **economy as a large dynamic nonlinear organic system** of closely interrelated and interdependent sectors dictating to the planners the necessity of strict inner coherence and consistency of the measures to be included in the plan. These intrinsic properties of consistency and coherence of the system to be subjected to planning found their most elaborate and explicit reflection in the demand structure. Therefore, it became the primary function of the planning bodies to first identify the demand structure in its details with as much precision as possible. Then, on the basis of its logic and movements, the planning bodies forecast and projected the trends perceptible in the market which could then be passed on to be used by the planners in the process of decision making concerning their respective areas of competence — sector or regions. They further stressed that, while drawing up the plans, the internal balance must not be disturbed as far as possible. Also, the inter-relationships between the various sectors should be so organised so as to keep the system in a state of general equilibrium. It was impermissible, in the view of the geneticists, to expand one sector, be it heavy industry or any other, without taking full cognizance of its likely impact on the equilibrium of the interrelated sectors. Ignoring the essential equilibrium conditions between sectors would eventually lead to creation of serious macro-economic disproportions, which would, in turn, impede the development of the economy as a whole.

This school of economic thought was closely involved with the planning process during the NEP and, hence, it favoured planning within a broad market framework. However, the ideas of this group regarding the role of and scope of planning were vehemently opposed by the other group of economists, the most influential economists in their ranks being P.A. Feldman (credited with developing the first mathematical model of unbalanced growth in favour of heavy industry) and S. Strumilin. The members of this group looked upon the planners not simply as economists following the dictates and constraints imposed by the market forces, but as qualitatively different kind of economic experts.

They would now be engaged in a qualitatively more complex task of engineering of the economic machine. It would involve overcoming the limitations put by the market forces on economic development and activities of the economic players involved including the state and finally changing the system itself. In short, they viewed the **planners as economic engineers and the economy as a machine**. This group of economists came to be known as the **teologists**. The leading role in economic development belonged to the plan which was to deal with the other sectors especially finance and market. The starting point for planning in their view was not the existing and projected demand structure, but the formulations of the national goals by the political leadership of the country. It was then that planners came into the picture. Their main function was formulation of an economic strategy which would include such parameters as output targets for basic industries, with the only limitations being imposed by the available amount of resources. These resources could be allocated to meet the needs of the various sectors, more importantly the heavy industry, independent of the market requirements. They did not consider the maintenance of equilibrium in the economic

system of any relevance in their model of planning, but looked upon it as an unnecessary constraint. According to them, the process of planning consisted of successive approximations: first plans for the crucial sectors were to be prepared, then the plans of the other related sectors, but secondary in importance in to the first ones.

12.3.2 Structure of Planning

There had been attempts at planning of the country's economy from the earliest days of the Soviet regime. These, however, were either extremely limited in their scope and did not play any significant role in the economic life of the country or were not implemented due to the war and overall disruption. In any case, for the whole period of 1917-28, there was no comprehensive economic planning, inspite of the communist leaderships' dedication to the goal of introducing planning in the development process in the country. However, it would not be correct to assert that there had been no planning at all. During this period considerable experience had been accumulated in formulation and implementation of plans, albeit, on small scale and usually within the different sectors when they were facing the shortages of inputs and foods by, credit crunch and difficulties in the distribution system. There were a variety of agencies which in one way or another were involved in drawing out of plans throughout the turbulent twenties. Among the most important were the Vesenkha (Supreme Economic Council), The Ministry (Commissariat) of Finance, The Ministry of Transport, the Gosplan of USSR (directly under the central authorities), the regional Gosplans, the Sovnarkhozy and other minor agencies were involved in the planning process.

The sole purpose of the Gosplan, a major agency among this great variety of government bodies, was to prepare long-term and operational plans. In the early twenties, the main burden of the work for coordinating the great variety of sectoral plans was placed with the Gosplan. But, apart from this function of an overall coordinator, the Gosplan had very little to do with the actual planning process even of the various sectors, which was relegated to sectoral administration. The work of planning was usually carried out either by the sectoral glavki or by the Vesenkha. The Gosplan participated in this process in the capacity of an agency providing the so called control figures or, in other words, tentative output targets for different sectors of the economy. The operational plans for the individual sectors which included financial and production targets with a detailed period wise break-up for the year known as **texpromfinplans** were being drawn up by the glavki and the Vesenkha. This period saw an important innovation in the planning methods with the introduction of a system of 'material balances' which consisted of the balance for the use of various industrial commodities, usually in short supply, in individual sectors. This system of planning which involved a large number of separate planning agencies proved to be too complex and cumbersome. Finally, the planning function was almost completely transferred to The Gosplan. Now the process took approximately the following form: The Gosplan, in its capacity as the central agency on planning, would first receive the proposals from all other planning bodies. Then the Gosplan would work out its own independent control figures for the development of the various sectors. Then the proposals from the other planning bodies were modified in accordance to the 'control figures' worked out by the Gosplan and the modified version of the original proposals were given the form of the 'texpromfinplans'. Finally, the allocations were made to individual sectors and enterprises in accordance with the balances drawn on the basis of modified versions of the 'texpromfinplans'.

Check Your Progress 2

- 1) Describe the planning controversy.

.....

.....

.....

.....

.....

2) Describe the process of plan formulation.

.....

.....

.....

.....

.....

.....

12.4 THE FIVE YEAR PLANS

The first control figures for the First Five Year Plan were initially prepared by the Gosplan in the form of a draft presented in March, 1926 for discussion. At first the implementation of the plan was to begin in 1926, but later it was postponed to 1927 because of the inability of the government to make a decision on the issues discussed earlier. Only later when the disputes had been resolved it became possible to present a properly drawn out plan for discussions and subsequent implementation subject, to the changes sought, if any.

Table 12.1: The First Five Year Plan

Variants of the Plan and Years	National Income	Non-productive Consumption		Gross Investment	Amortisation	Accumulation in both Fixed and Working Capital		Growth of Fixed Capital	
		In % of Col. 2	In % of Col. 2			In % of Col. 2	In % of Col. 2		
1	2	3	4	5	6	7	8	9	10
1927-8	24.7	20.0	80.1	7.99	3.33	4.66	18.9	3.72	15.1
Minimal variant									
1928-9	27.5	21.3	77.4	9.70	3.48	6.22	22.6	4.64	16.9
1929-30	30.5	22.8	74.9	11.37	3.70	7.67	25.1	5.84	19.1
1930-1	33.5	24.5	73.0	13.04	4.00	9.04	27.0	6.87	20.5
1931-2	36.9	26.7	72.4	14.58	4.38	10.20	27.6	7.68	20.8
1932-3	40.6	29.6	73.0	15.76	4.81	10.95	27.0	8.54	21.0
For the five years	169.0	124.9	73.9	64.45	20.37	44.08	26.1	33.57	19.9
Optimal variant									
1928-9	27.5	21.3	77.4	9.70	3.48	6.22	22.6	4.64	16.9
1929-30	30.9	22.2	71.8	12.41	3.70	8.71	28.2	6.47	20.9
1930-1	34.8	23.6	67.9	15.22	4.04	11.18	32.1	8.23	23.6
1931-2	38.7	25.8	66.8	17.34	4.49	12.85	33.2	9.39	24.3
1932-3	43.3	28.8	66.4	19.55	5.01	14.54	33.6	10.96	25.3
For the five years	175.2	121.7	69.5	74.22	20.72	53.50	30.5	36.69	20.9

(Source: Maurice Dobb Soviet Economic Development since 1917, London, 1960 p. 236.)

12.4.1 The First Five Year Plan

The First Five Year Plan was projected in three different scenarios or 'variants'.

- I. There was the maximum variant or the worst case scenario, taking a cautious approach to the various uncertainties that may manifest themselves in the course of the plan implementation and be a source of setbacks.
- II. then there was the optimal variant taking a balanced look of the possibilities and the uncertainties for the development process in the future and,
- III. lastly, there was the maximum variant or the best case scenario, which was based on assumption that the uncertainties in the future would not have a very serious negative impact on the development efforts. A table, which has been borrowed from chapter 10 of Maurice Dobb's book mentioned in section 'Some Useful Books', of the minimum and the optimal variants is given below. (Table 12.1)

Taking an overall view of the economic development during the whole period of the First Five Year Plan, it becomes clear that, in spite of many negative developments, this period can be considered to be one of economic success, fulfilling the major objectives which the government and the Communist Party leadership had set before themselves. One of the major problems which the government faced during this period was that of excessive labour in the towns accompanied by a shortage of qualified working hands and trained personnel. This posed a serious problem, not only because a steep increase in the population in the towns gave rise to many problems related to housing, medical services, etc., but also because the shortage of trained workforce would exert severe constraints on supplying the growing modern industrial sector with technically educated personnel and managerial staff. The excess of the untrained worker was a result of an influx of labour from the countryside.

The events of the first two years of the First Plan were on the whole considered to be fairly successful, though they certainly were not without many negative features. Among the positive gains of this period was a substantial increase in the yield of technical crops. Also, collectivisation moved ahead at an impressive pace. But on the negative side there was disequilibrium between demand and supply about which Bukharin and his associates had warned long ago; it not only persisted but, in fact, got accentuated even further. But the overall development during the next two and a half years was considerable. The most important result was the considerable increase in the rates of investments, which even surpassed the original estimates. The negative side of this success was that this increase took place at the expense of investments in the light industrial sector, thereby impeding its development and slowing the pace required to satisfy the demand for its products. Other small scale sector enterprises and workshops, along with private agriculture were the areas to suffer because of exceptionally high rate of investments in the heavy industry. But the State Machinery Stations provided agricultural equipment and machinery to the collective farms and State farms. So these were the main beneficiaries of discriminating investment policy of the government, which had favoured these branches with considerable investments at the expense of the sectors mentioned above.

During this period, a large number of industries were reconstructed on the basis of new equipment and machinery, produced during the plan period itself. Thus it, was estimated that about 50 to 80 per cent of the new equipment and machinery was introduced in engineering, coal mining, motor car and tractor building, and machine tool construction. Some sectors had such a high proportion of newly created capacities that they could have been described as newly constructed industries. Chemical, oil refining and energy industries were precisely such sectors. The industries belonging to Group A, which included all the industries engaged in the production of capital goods or "industries producing means of production" in Marxist economic terminology, were among those that showed particularly good results, in many cases showing results even better than the figures projected for them. They outstripped the projected figures for these industries by a margin of about 250 per cent. The large scale industry, considered on the whole, showed a growth of 118 per cent over the 1926-27 level, falling slightly behind the projected target of 133 per cent, while the oil industry showed a marginal positive difference in comparison to the projected figures of the plan.

The consumer goods sector or the Group B of the industries in the Marxist economic terminology showed results which could not by any means be called even satisfactory — their performance was simply poor. The textile industry was certainly the poorest performer. This branch of the light industrial sector showed a decline in production in certain areas even below the production level of 1928. The food catering industry, however, showed remarkable progress especially in building canteens and factory dining-rooms ('stolovayas') for the workers, thereby contributing greatly to raising the standard of life of the workers. At the end of the plan, this sector expanded to a scale when it could provide at least one meal per day for approximately three-fourths of the workforce.

The State Budget was the main source for raising the level of investments. In the plan, the investments were envisaged to be generated by the reserves of the industry itself by cutting down on the costs, but that aim remained mainly unfulfilled. After 1930, the financing of capital investments and investments in the defence industry was carried out by generating finances through imposition of a turnover tax, which was determined in proportion to the volume of the turnover.

The overall conditions of life remained difficult, in spite of fairly good overall performance of the economy. It became clear that the persistent efforts in the construction sector and industry would have to be continued in order to bring about a really tangible change in the standard of life of the mass of the population, not only for a section — represented by the urban workers, especially the highly qualified section of the workforce. But at the same time signs of a better future were already discernible by the end of this plan period.

12.4.2 The Second Five Year Plan

The Second Five Year Plan began in 1933. The major thrust of this plan was towards completing the work on technical reconstruction of the economy begun under the previous plan. During this period, the main direction of the plan was to consolidate the gains of the previous plan, which found its reflection in

- a more modest target setting
- increased emphasis on qualitative improvements in the work methods and work ethics,
- increased productivity of labour by improving the quality and intensity of work and
- cutting down of overhead costs.

However, it was realised that success in this direction depended on specific measures which had to be taken towards introducing new and/or improved methods of production and new techniques. Therefore, the planners set lower output targets in the final plan document than in the draft version, and concentrated particularly on the qualitative aspects of the economic activities rather than on the in magnitude.

Agriculture was subjected to radical changes during this period, especially by establishing new relations between agriculture and industry, and replacing the market system by a system of planned supply quotas. As we have seen, the forward contract scheme, initiated earlier, provided that the payment for services rendered to the collective farms by the government or its enterprises could be made later at the harvest time, on the basis of certain guaranteed supply quotas by the collective farms. During the Second Plan, this form of contract became dominant, and the supply quotas which were earlier made on a voluntary basis were now made obligatory. The prices of agriculture goods were fixed by the government. For the collective farms, a special concession was made, whereby they could sell in the market place the surplus left over and above the quota fixed by the government.

A very significant consequence of this system was that, as the quotas were fixed beforehand, the collective farms were now more interested in maximising their production, because a larger yield would leave them with larger stocks after the deduction of the quota. This led to an increase in the marketable surplus and consequently to greater availability of food products to the urban centres and raw materials to the industry. This achievement was even more commendable because of the rapid rise of the urban population and was high rates of growth of industry. It was estimated that the amount of the surplus available for consumption to the urban centres and to the industry increased during the decade 1928-1938 by approximately 250 per cent.

In the **industrial sector** the main emphasis was now on improving the performance of the iron and steel industry by introducing new technologies, and training of personnel capable of working with these new technologies. In addition, the development of the non-ferrous metal industry was also put on the agenda of the plan. This would reduce substantially the dependence of the country on imports of these crucial industrial basic inputs the demand for which was rising steeply as a result of the development of electrical and defence sectors. These industries put a particularly heavy demand on such non-ferrous metals as copper, aluminium, zinc and nickel. The products production of copper was to be developed in the Ural and in Kazakhstan, the latter also being developed as the major lead producing area along with the zinc producing areas.

The production of a range of non ferrous metals was set up in the country for the first time. The production of nickel, magnesium and tin was included in the plan for expanding the base of metal production in the country.

The transport sector was another area, which was given high priority in the development policy of the Second Five Year Plan. This sector was under severe strain at the time due to a number of reasons, and had become a major bottleneck for the economic growth in general. Only large investments in this sector would enable the economy to function smoothly. This strain was a consequence of the industrialisation and the subsequent migration of large numbers of people from the villages to the towns and cities. Apart from substantial increase in the movement of foodstuff from the countryside to the urban centres, there was a considerable change in the pattern and volume of interchange of materials between the different regions of the country. The road transport, by and large, barring the immediate vicinity of large towns, was in a very poor condition. The river transport was also in no better condition as far as its technical base was concerned. For, major parts of the country were equipped with extremely poor hardware and harbour and port facilities were, if anything, primitive. The railroad was interconnected by a single track, which, in its turn acted as a constraining factor in the movements of industrial and agriculture products. The hardware base of the railways — at stations, signalling systems, depots and repair equipment — was largely inadequate and obsolete.

The engineering and machine tool industries were also made the focus of attention on the part of the planners as it was realised that qualitative changes in the production sphere and higher productivity were largely dependent on establishing a technically modern base for the enterprises in these crucial sectors. The Second Plan, therefore, attempted to considerably increase the availability of modern machinery and other equipment — production of approximately 200 new types of machine tools was designed to be set up. This was considered to be central element in the overall design of creating a new machine building sector in the country, ensuring a highly developed sector for producing machines. The planners concentrated their efforts in this sector mainly on setting up production not only of modern and technically superior machine tools but, wherever it was possible, they gave preference to production of complex machine tools, and more importantly to the production of automatic and semi-automatic machines.

One of the overriding concern, of the planners was that the development of this sector should proceed at such a paces and be concentrated in those areas of crucial import, which would make it possible for the country to become independent of foreign sources in the shortest possible period. Thereby undue strains of importing machinery as it happened during the First Plan period would be avoided the barrier to faster growth in the future not only of industry, but of the rest of the related sectors as well would be removed. The increase in the production in this sector in value terms was estimated to have been to the extent of 500 per cent. The explanation for such a steep rise in this indicator lay in the fact that a large portion of the output consisted of complex machines integrating the latest technical innovations. On the other hand, the increase in physical terms or real growth was much less and constituted approximately 250 per cent over the level of the previous plan.

The rationalisation of the regional (or territorial) structure of production in accordance with the requirements of the time was another salient feature of this plan. Though considered an integral part of the planning model and the need for which was emphasised even in the early twenties, it was in fact now forced upon the planners due to the strain put on the economy by the relative underdevelopment of transport system, which hindered smooth movement of the products between the regions and made the delivery and supplies of goods extremely erratic and uncertain. The industries using large quantities of raw materials but in which a large portion of weight of the raw materials is lost during processing and production of the final product, the so called weight losing forms of production such as metallurgy, were now planned to be shifted to major mining regions. This eventually marked the beginning of the eastward shift of the industries using raw materials in bulk as the East was the main mining area for minerals and metal ores, and initiated a process of accelerated development of the once backward areas of Siberia and Kazakhstan and also of central Asia which was to become an area of specialised technical crop cultivation. This policy was all the more enthusiastically persued by the Soviet government as its objectives coincided with the objectives of the Nationality policy of accelerating economic, and more particularly, industrial development in the erstwhile colonies of Imperial Russia. The policy, as officially stated envisaged a more even distribution of the productive forces over the country for overcoming the social, educational and economic backwardness of the national republics and regions.

2.4.3 The Third Five Year Plan

The Third Five Year Plan began in 1938 under very special and grave circumstances, not only for the Soviet Union but also for the whole of Europe, as the Nazi Germany was preparing for war, and eventually it was the German attack which put a stop to all economic development of the Soviet Union for a long time to come. It is very difficult to state categorically to what extent the third plan was influenced by the requirements of the defence preparedness of the USSR — what would have been the structure of allocations and the priorities of the planners, had the war not loomed so large over the whole of Europe. Transport, chemical and heavy industries were the main thrust areas. The emphasis was again on the development of heavy and defence industries, light and consumer goods industries being again neglected.

It was expected that the growing industry and migration would continue to exert pressure on the transport system, and that the existing capacity would prove inadequate to cope with the demand generated by an expanding economy for the services of the transport sector. Thus, in the Third Plan, major improvements were to be conducted in the railways in terms of extension of tracks and technical upgradation. The first estimates included an increase of about 7000 miles in the total mileage of the railway tracks. A considerable portion of the mileage was designated to be converted into double tracks. The target for the double track was set at 5000 miles. Over one thousand miles of tracks were now planned to be electrified.

As mentioned earlier, the light and consumer goods industries were the main losers. It is estimated that of the total investments which were set aside for the industrial sector as a whole, only about 15 per cent, the same as under the First Plan, were diverted to the light industry. The light industry, as a result, could show only a modest growth; its output showing an increase of 69 per cent over the period. Apparently the threat of war and the need for accelerated armament restricted the planners' choices and they were forced to postpone the shift in the investment structure during this period in favour of the light industry. The resources which would otherwise have gone towards increasing the capacity of the light industrial sector, were now reverted to expanding the capital equipment in the heavy industry.

The overall economic results for this period cannot be characterised as substantial. On the contrary, they seem to be very modest when they are compared to those of the preceding decade, and especially the Second Plan. During the three year period of the Third Plan, the total national income increased by 30 per cent. The growth rates of many industries showed only a marginal increase over the rates characteristic for the first two plans — the production of steel in 1940 remained at the level of 1938; the output of pig iron and oil also showed marginal increase over the level achieved by the end of 1938. The industrial output could only show an increase of 14 per cent per annum. The industrial sector, as a whole, could only show an increase of 44 per cent in its gross output over the three year period, the break up between the heavy industry and the light industry (group A and group B industries) being 50 per cent and 33 per cent respectively.

12.5 LET US SUM UP

During the period immediately preceding the First Five Year Plan, the economic conditions had eased to an extent which allowed the government to attend to the task of radically changing the foundations of agriculture in the country. The purpose was to transform it into a highly productive large scale sector utilising modern methods, equipment and machinery. There were deep divisions in the party on this issue, which as the events showed were, in fact, divisions on fundamentals of economic development. The supporters of the large scale collective agriculture finally prevailed, and the government initiated the process of collectivisation of agriculture, which was to have far-reaching consequences.

Simultaneously, serious discussions were being conducted on the issue of the role of planning in their development process. In the course of these discussions, two basic paradigms of planning were formulated: the first one considered that planning must be directed by consumer demand and conducted in a broad market framework; the other,

on the contrary, proposed planning to be directed only by the objectives set by the government, trying to overcome the market constraints in the process. In the final analysis, the second group prevailed and the system of a centrally planned economy, thus evolved came to be known as the command economic system.

The implementation of the National Plans started in 1928 and continued uninterrupted up to the outbreak of the war with the Nazi Germany in 1939. This period was one of great difficulties, but also of spectacular achievements, especially in developing the heavy industry base of the economy. On the whole the Soviet Union remained far behind the industrialised countries of the West, but the gap dividing them was progressively closing down.

12.6 KEY WORDS

Artel: A system in which the member peasants conducted their farming collectively and shared the yield from the agricultural land which was now held in common with commonly owned implements, while their houses and house gardens continued to belong to each member separately.

Geneticists: Economists who supported planning within a broad market framework.

Sovkhozy: State owned farms.

Teologists: Economists who supported the primacy of planning.

Texpromfinplan: Operational plans for the industrial enterprises.

12.7 SOME USEFUL BOOKS

Carr E.H., and R.W. Davies, 1969, *Foundations of a Planned Economy*, Vol. 1 and 2, London.

Dobb, Maurice, 1960. *Soviet Economic Development Since 1917*. London.

Erlich, Alexander, 1960. *The Soviet Industrialisation Debate: 1924-1928*, Cambridge.

Jasny, Naum, 1961. *Soviet Industrialisation: 1928-1952*, Chicago.

Jasny, Naum, 1949. *Socialised Agriculture of the USSR*, Stanford.

12.8 ANSWERS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) Read section 12.3 to answer
- 2) Read section 12.3 to answer

Check Your Progress 2

- 1) Read section 12.4 to answer
- 2) Read section 12.4 to answer

UNIT 13 RATE, STRUCTURE AND SPREAD OF MODERN ECONOMIC GROWTH

Structure

- 13.0 Objectives
- 13.1 Introduction
- 13.2 Epochal Innovation : The basis of Modern Economic Growth
 - 13.2.1 The Application of Science to Economic Problems
 - 13.2.2 Attitudinal Changes in Fostering Science
- 13.3 Modern Economic Growth: Definition, Measurement and Associated Problems
 - 13.3.1 Modern Economic Growth : The Concept
 - 13.3.2 Measurement of Economic Growth and the Problems Associated with it
- 13.4 Rates of Growth and Its Time Pattern
 - 13.4.1 Kuznet's findings on rates of growth
 - 13.4.2 How Sustained were the Rates of Growth
 - 13.4.3 Were High Rates of Growth Peculiar to this Epoch?
 - 13.4.4 How long are these High Rates of Growth Maintained?
 - 13.4.5 Behaviour of Population Growth during Epoch of Modern Economic Growth
- 13.5 Modern Economic Growth : Changes in Industrial Structure
 - 13.5.1 Statistical Evidence
 - 13.5.2 Changes in the Various Sectors during Economic Growth
 - 13.5.3 Trends Explained
- 13.6 Inter-Sectoral Inequalities During Modern Economic Growth in DCs and LDCs.
 - 13.6.1 Reasons for Higher Labour Productivity in Services Sector
 - 13.6.2 Inequality in the size-Distribution of Income
- 13.7 Modern Economic Growth : Other Trends in the Economic Structure
 - 13.7.1 Changes in Distributional Aspects
 - 13.7.2 Three Other Trends in Modern Economic Growth
 - 13.7.3 International Flows of Men, Goods and Capital
- 13.8 Spread of Modern Economic Growth
 - 13.8.1 Was the Spread of Modern Economic Growth Limited?
 - 13.8.2 Why Did Modern Economic Growth Originate in England?
 - 13.8.3 The Transition Period in the Spread
 - 13.8.4 The 'Follower' Countries
 - 13.8.5 An Alternative Framework For Analysing the Spread
- 13.9 Let Us Sum Up
- 13.10 Key Words
- 13.11 Some Useful Books
- 13.12 Answer/Hints to Check Your Progress Exercises

13.0 OBJECTIVES

The study of economic growth of a Nation or a region, which means a sustained increase in the capacity to provide goods, is important—not only to know the rate of increase of the output given an increase in capacity but also the mechanism by which this rate is realised, sustained or impeded. This unit aims at acquainting you with modern economic growth of nations : its rate, structure and spread which is a distinctive phase in the history of eco-growth.

After going through the unit you will be able to:

- describe how western societies grew in material well-being over the last one and half to two centuries,
- discuss the mechanism which made it possible to achieve such high rates of growth in product per capita to signify it as a distinct epoch called the modern Economic Growth.

- and analyse why this rapid growth was limited only to the present day developed countries and did not spread in equal measure to the presently developing countries.

13.1 INTRODUCTION

Modern Economic growth has been identified as characterised by sustained increase in per capita or per worker product. This increase has most often been accompanied by an increase in population and usually by sweeping structural changes which simultaneously raised the productivity of the population. If therefore, modern economic growth implies marked rises in product per labour unit when population and, therefore, labour force are increasing it must be possible only through some major innovations. The natural question to answer here is, therefore, what are these rates and what is that innovation that has been exploited during this period? The epochal innovation that distinguished the modern economic growth is the extended application of science to problems of economic production. But before that, we take a look at the changes that has accompanied this innovation.

Modern economic growth based on application of science has given rise to what we now call significant, orderly and distinctive body of long term economic experience. In contrast to the earlier periods, in modern times, on the basis of quantitative characteristics, it has been observed that modern economic growth has given rise to the process of industrialisation that went hand in hand with the process of urbanisation; besides this, the other characteristic features associated with modern economic growth that have been observed are:

- a) In the relative economic position of groups within the nation distinguished by employment status, attachment to industries, level of per capita income etc. etc.;
- b) In the distribution of product by use among household consumption, capital formation; towards innovation and basic sciences etc.
- c) In the allocation of product by its origin within the nation and elsewhere; and
- d) In the effect on economic growth of one nation on that of another.

In the rest of the Unit, therefore, we first discuss the meaning and measurement of economic growth alongwith the problems associated with its measurement, then bring together the basic characteristics of modern economic growth during the last one and one half to two centuries.

Besides high rates, the characteristics of modern economic growth upon which we shall dwell include industrial structure of labour force and National product, capital formation proportions (both cross section and long term trends), and finally the expansion in the volume and proportions of international flows of men, goods and capital. Discussion of trends in industrial structure would relate to:

- a) the changing proportion contribution of the major sectors to aggregate product and their changing shares in labour force and other productive factors. Specifically, three shifts in productive structure, associated with modern economic growth are highlighted. First, the movement of labour away from agriculture due to high agricultural productivity usually referred to as industrialisation: second the change in structure within industry proper; and finally shifts in structure in the service sector.
- b) Distribution of product and income. The discussion here deals with trends in factor shares as well as distribution of personal income by size for the developed countries and how that distribution supports the industrialisation process.
- c) Broad classes of product use: household consumption, government consumption and capital formation.
- d) International aspects of modern economic growth: the discussion relates to inter-dependence among developed countries and between them and the rest of

We shall bring the study of modern economic growth to an end by considering the questions about its spread. Specifically, we shall try to show higher growth made possible higher diversion towards basic sciences which through its application gave rise to still higher rates of growth, but rate of its spread, however, remained slow.

13.2 EPOCHAL INNOVATION: THE BASIS OF MODERN ECONOMIC GROWTH

The word 'modern' typifies the period of the last two centuries and possesses distinctive characteristics which give it unity and differentiate it from preceding periods. Economic historians identify such periods on the basis of certain innovations which provide a potential for sustained economic growth. Such innovations are so major that their exploitation and utilisation absorb the energies of human societies and dominate their growth for a period long enough to constitute what they call epochal innovation.

13.2.1 The Application of Science to Economic Problems

The epochal uniqueness that distinguishes modern economic epoch is the extended application of science to problems of economic production. We may call this long period 'the scientific epoch' in which countries not only witnessed the growth of basic sciences but also its application through changes in social organisations.

The history of civilisation tells us that most of humankind lived in poverty for thousands of years. Primitive technology of handicrafts and cottage industry were inadequate to meet the basic needs of everyone. The estimated growth rate was one per cent per century.

In the pre-modern era, simple trade, and somewhat later merchant capital dominated. With the changing times, usury and trade were supplanted by capital. In the 18th century mass production of goods started in a small area of England inhabited by less than three million. The beginning of mass production of goods in England is known as the start of industrial revolution. The industrial revolution was begun with invention of the based on the steam engine, the spinning and weaving looms.

Later, discoveries in physics, chemistry, mathematics and biology led to the application of science in industries based on iron and steel, cotton fibre, petroleum, power transmission, agriculture, medicine, energy and earth sciences. This was followed by technologies of mass production based on electric power, liquid fuel, radio waves, X-ray, Internal Combustion engine, electric motors.

Specifically, since the second half of the nineteenth century, the major source of economic growth in the developed countries has been science-based technology in the electrical, internal combustion, electronic, nuclear and biological fields, among others.

From England, industrial activity spread to European countries and then to USA and Nordic countries. Japan and USSR appeared on the scene during the depression of 1930s. In the post world-war II world, China, India, Indonesia, Brazil, Egypt and many countries of Eastern Asia joined in such industrial activity in a big way. One of the important features of this horizontal growth throughout has been application of science and scientific method in improving technology and production methods. The gap between science, technology and production has gradually been considerably reduced. Scientific and technology based methods of production have continuously and cumulatively improved and new ones replaced the older processes. Hand tooling by mechanical-electrical-electronic and bio-technical methods in that order. The result of all this has been improvements in the quality of the inputs used in production.

The application of science, however, requires a proper climate of human opinion in which both the pursuit and use of science can be fostered. Thus when we say that the

modern epoch is distinguished by application of science to problems of economic production and human welfare we also imply that it is distinguished by a climate of human opinion, by some dominant views on the relation of man to the universe that foster science and its application.

Application of science via technology, therefore, requires changes in social institutions. New attitudes are needed to accommodate and foster adjustment of social institutions and practices to the exploitation of the potential provided by science-based technology. What are these attitudes?

13.2.2 Attitudinal Changes in Fostering Science

The broad views associated with the modern economic epoch suggested by Kuznets can be summed up in three terms: secularism, egalitarianism, and nationalism.

By secularism we mean concentration on life on earth as man's main concern, economic attainment being assigned the highest rank in this state of priorities. By egalitarianism, we mean denial of any inborn differences among human beings. This makes man a full-fledged participant in the community of men. Nationalism is the claim of community of feeling, grounded in a common historical past and its cultural heritage.

The epochal innovation that underlines modern economic growth spread very fast because of the acceptance of the above three as the way of life by the majority of humankind. However, it may be kept in view that (a) there may not necessarily be sharp breaks between economic epochs; and (b) even in modern times economic growth may not necessarily be science based.

For example, although British revolution was the first in history this in any case does not mean that it started from zero, or that earlier phases of rapid industrial and technological developments cannot be found. In fact British revolution was preceded by at least two hundred years of fairly continuous economic development, which laid its foundation. Unlike say, nineteenth century or twentieth century Russia, Britain entered industrialisation prepared and not unprepared. Also it is observed from economic history that some of the economic growth in modern times was due to a slow, trial-and-error process of learning. The partition of Africa late in the nineteenth century was, so to speak, a postscript to merchant capitalism within the new epoch, made possible by the steam railroads. Conversely, science based technological changes took place in earlier epochs also.

Furthermore, neither secularism nor egalitarianism is all-pervasive, even in the economically most developed countries; nationalism varies greatly in intensity, showing no close positive correlation with economic development. Therefore, all that we mean here is that science-based technology and the broad views needed for its successful exploitation by human societies were so dominant in the countries that sustained modern economic growth as to constitute a distinctive feature of the modern economic epoch.

Check Your Progress 1

- 1) What is the basis for calling the modern economic epoch 'the scientific epoch'? Give some illustrations.

.....

.....

.....

.....

.....

.....

- 2) What were the main attitudinal changes that one associated with modern economic epoch?

.....

.....
.....
.....
.....
.....
.....

3) Briefly explain the concept of modern economic growth?

.....
.....
.....
.....
.....
.....

13.3 MODERN ECONOMIC GROWTH: DEFINITION, MEASUREMENT AND ASSOCIATED PROBLEMS

Economic growth of a nation generally speaking means a sustained increase in its output of goods and services. The increase must be sustained over a period long enough so that it reflects more than a cyclical expansion or an unusually large harvest, or a post-calamity recovery or some other transient rise.

13.3.1 Modern Economic Growth: the Concept

This definition is, however, quite general. An being so general it is not useful to the explanation of economic growth of nations in modern times, i.e. during the last one and one half to two centuries. Modern economic growth of nations has two distinctive features. Firstly, in all countries it involved a sustained and substantial rise in per capita product and secondly, in all cases it involved a sustained and substantial rise in population also. We, therefore, taking these features into account define economic growth as a sustained and substantial increase in per capita product often accompanied by substantial increases in population, and its productivity.

In this definition you see that we say **sustained** and **substantial** rise. The emphasis on a sustained and substantial rise particularly in per capita product is important because it has implications for both the structure and conditions of modern economic growth. For example, a cumulatively large rise in a country's per capita product necessarily means a shift in relative proportions of various goods demanded and used under given structure of human wants. It also means a major changes in combination of factor inputs, in patterns of lifestyle and in international relations. Also a rise in per capita product usually means an even larger rise in product per unit of labour input if population is also simultaneously rising.

Marked rises in product per labour unit, when population and, therefore, labour force are also increasing, would usually be possible only through major innovations. We, therefore, identify modern economic-growth based on a system of production which makes increasing use of modern scientific knowledge. For we know if large increases in product per unit of labour are to be achieved it must be possible only through increased efficiency of inputs used. These are only possible by the use of improved technologies based on modern science.

Scientific knowledge continuously change such that older methods are replaced by new technologies. This has implications for the structural changes in the industrial

system. New industries would appear and old would recede in importance. This in turn would call for the capacity of society to absorb such changes. Thus in the study of modern economic growth rise in per capita product is emphasized because of its implications for structural changes that originate in technological innovations and society's capacity to absorb such changes—changes in attitudes.

13.3.2 Measurement of Economic Growth and the Problems Associated with it

We have seen above that modern economic growth implies sustained rises in per capita product. We have also shown that it leads to major structural changes and correspondingly large modifications in social and institutional conditions under which the greatly increased product per capita is attained. Therefore, for purposes of measurement of modern economic growth the changing components of the structure need to be reduced to a common denominator. For, otherwise it would be impossible to compare for example the product of the economy of USA with that of China or for that matter the product of an advanced country today with its output a century ago. This is because many of the goods and industries that flourish today were unknown a century ago.

Reduction to a common denominator of the changing components of the structure calls for decisions regarding what to include and what to exclude, i.e. the question of scope, the question of netness and grossness and the basis of valuation of output which are usually treated in discussing conceptual problems in the measurement of national product. The other conceptual problems relate to subdivisions by industry of origin, factor and type of income, type of use, i.e. consumption and investment and domestic and foreign origin of output etc. All these concepts and their associated problems are already known to you as part of your first lessons in economics in your preparatory, foundation and first elective course in economics.

In those lessons we have told you that numerous problems arise when we attempt to reduce national product of differing compositions, originating under different social conditions to comparable aggregates that are divisible into additive parts. In these lessons we also gave you in detail the methods employed. Here we only enlist the major assumptions on which these thorny and essentially insoluble problems are usually resolved in actual measurement.

The basic assumption in reducing output to a common denominator relates to the weights that are attached to various outputs or productive factors. In that we assume that these weights are taken from one or a few societies and have meaning for all or atleast for most of them. This assumption facilitates comparisons over space as well as time. For if we do not assume this and instead accept that people today are radically different from their forbearers of fifty to hundred years no meaningful comparison over time would be possible. Similarly, if we assume that the inhabitants of USA and those of Russia are so different that food, clothing or labour and capital goods mean quite different things to them, comparison of the national product of the two countries likewise would be impossible.

In actual application, therefore, weights employed should be those of one or a few economies or of one or a few points in time; of the more developed rather than the less developed economies and of the more recent point of time rather than the earlier. An example of such an approach in the international comparison is found in the united nations estimates. It was based on the use of the purchasing power of USA dollar and has been generally followed since then by all concerned with this problem.

Likewise in the measurement of changes over time, output is usually expressed in constant prices of recent years and not in prices of the past. The rationale for such choices, over and above the greater availability of data for advanced economies, and for recent years lies in the fact that economic growth is generally evaluated from the vintage point of the higher levels already attained. Moreover, we live today and not in the past and the less advanced economies aspire to the levels of the more advanced and not vice-versa. Therefore, more advanced economies and the more recent times are best suited to the evaluation of economic growth.

The use of weights and concepts typical of advanced economies or of recent times have been criticized as they generally introduce a bias into comparisons. It is argued that the bias is such that it favours more advanced units or more recent periods. Here, there may be an upward bias due to: (a) the exclusion of the non-market bound activities. These are proportionately more in less developed than in more advanced countries, and in earlier than in more recent decades; and (b) the measures of output also do not make full allowance for the costs of the higher levels of output, greater costs of urban life etc., which are proportionately greater for advanced economies and for the more recent times. While this is true we should, however, not ignore that there are factors which make for a downward bias also. For example, the use of recent price weights tend to yield a lower rate of growth. Likewise the use of the price weights of the advanced countries tends to give many raw materials and simpler goods in the under developed countries higher standing than in fact they have.

Thus, it is not true that the common basis of valuation and treatment in international and intertemporal comparisons produces a bias that favours uniformly the more advanced economy or the more recent time only. In act these procedures under-estimate the differences across space or in the rate of growth over time. The problems of measurement will, however, continue to plague the statistical work. This, however, does not mean that the conceptual and other difficulties of measurement justify the refusal to measure for the empirical corroboration and testing. Therefore, without waiting for such time when we can resolve the statistical problems of index numbers which are used to reduce output to common denominator the empirical testing of economic phenomenon can be done subject to these problems.

Check Your Progress 2

- 1) Mention Kuznet's main findings with regard to rate of growth of population, per capita income and total product in his sample of 19 countries.

.....
.....
.....
.....
.....

- 2) Why did not population growth accompany economic growth in the modern economic epoch?

.....
.....
.....
.....
.....
.....

- 3) What general observation can be made regarding whether the high rates of growth which are displayed when a nation enters into the modern epoch or not?

.....
.....
.....
.....

13.4 RATES OF GROWTH AND ITS TIME PATTERN

The experience of what we now designate economically developed countries show that the rate of increase in population, per capita product and total product in these

countries, over a period that extends over one and one half century since the industrial revolution in England, were unusually very high; not found in pre-modern periods. This is corroborated by Simon Kuznet's study.

13.4.1 Kuznet's Findings on Rates of Growth

Kuznets, in a sample of 19 countries, mostly developed, which covered roughly one third of the total world population and about one-fourth of the total number of countries of the world, found that for population, rate of increase ranged from 6 to over 20 per cent per decade. For per capita income the rates ranged from close to 10 to well over 20 per cent per decade. The rate of increase in total product was even higher. It never fell below 10 per cent per decade and ranged in most cases from 15 to over 40 per cent per decade. These rates were based on a time period of over half a century terminating in mid twentieth century in majority of the 19 countries. (See table I).

The pattern of growth, as observed by him, for the rest of the world, however, revealed a very startling fact. In purchasing power of the mid-twentieth century roughly half of the world population exhibited no more than 100 dollars per capita per annum income levels. This indicates that the rate of growth in per capita income over earlier decades in these countries could not have been very substantial. This shows that since the industrial revolution the industrial system spread to only a limited part of the world implying that the impact of technological and social changes that emerged from the industrial system did not advance the economic performance of the rest of the world to levels any where near those for most of the developed countries.

Having seen the rates and pattern of modern economic growth our next task is to see if these rates of growth can indeed be said to be very high: peculiar to this period only, and that if these rates exhibit some time pattern. This can be very easily answered by the following simple arithmetic calculation and the fact that science based technologies grew very fast during this period.

13.4.2 How High and Sustained were the Rates of Growth

A simple arithmetic calculation shows that if a rate of increase of 10 per cent per decade is sustained over a century, it means a rise to 2.6 times the initial value. The same over two centuries would cumulate to 6.7 times the initial value. Similarly, a rate of 20 per cent per decade will cumulate to 6.2 times the initial value over a century. In six of the 19 countries considered by Kuznets the rate of increase in per capita income was close to 20 per cent per decade and in four of these countries the period covered was very close to one century. Clearly these rates then would be very high which defy anybody's imagination.

That these rates were exceptionally very high can also be seen by extrapolating the observed rates backwards. If these were not exceptionally high rates then backward extrapolation of these will tell us that these countries will reach very low level of per capita income **too fast** to be historically true. For example, the extrapolation backward will give per capita income of 100 dollars in 1952-54 prices for most of the developed countries by the late 18th, early 19th or even the middle of the 19th century. Certainly, per capita income in UK in 1780 and in USA in 1795 was much higher than this level.

13.4.3 Were High Rates of Growth Peculiar to this Epoch?

The second question that these rates of growth were peculiar to this period only is corroborated by the historical evidence of the fast changing technologies based on science during this period.

A sustained high rate of growth cannot be achieved unless there is continuous emergence of new inventions and innovations. Only such a situation will provide the basis for new industries with high rates of growth to compensate the inevitable slowing down in the rate of growth of the older industries based on earlier inventions and innovations. Considerable shifting in relative importance among industries on balance will thus give rise to a high rate of overall growth in an economy.

We have already told you that there has been a tendency for scientific discovery, invention and innovation to concentrate at any given time in a few fields. To repeat here we refer you to the example of iron, steam and cotton textiles in the late 18th and early 19th century; electric power, communication and internal combustion engine in the late 19th century and Atomic energy replacing steam and electric era in the mid 20th century. The evidence both empirical and historical if taken together would reveal that without science based technologies and inventions these rates would not have been possible. In other words, science based technologies and inventions were necessary conditions of modern economic growth.

13.4.4 How long are these High Rates of Growth maintained?

The third suggestion that needs to be answered relate to the time pattern. Specifically, what we need to answer is; do the high rates which are observed when a nation enters into modern economic development maintained or do they decline and what are the reasons to expect such a systematic pattern?

The answer to this question will differ for various components of an economy; between old and settled countries and young countries. Nonetheless, some general observations can be made. The time pattern of growth in total product is a compound of those in growth of population and per capita product. Acceleration in the rate of growth of population, provided the rate of growth of per capita product does not decline, would necessarily produce acceleration in the rate of growth of total product. It would be further accelerated when the growth in the per capita product quickens. When both population and per capita product stabilize at a constant rate of growth, total product will also grow at a constant rate. When retardation in the rate of population growth begins, the growth of total product will be retarded, unless the rate of growth of per capita product begins at that point to accelerate which is highly unlikely. Thus, one may expect a long secular swing in the rate of growth of total product. Its phases of acceleration, constancy and retardation will follow the timing of the same phases between those for population and per capita product.

We know that the spread of the industrial system, since the eighteenth century was based on the additions made to scientific knowledge. This would imply much higher rates of growth of population, per capita product, and total product than before. At some period in the transition from pre-modern conditions to modern economic growth, therefore, there is likely to be a shift from lower to higher rates of growth. These shifts are, however, rarely, if ever, sudden. There would thus be substantial period during which the rate of growth would accelerate.

13.4.5 Behaviour of Population Growth during Epoch of Modern Economic Growth

Acceleration in the rate of growth of population occurs largely because new technology has the most immediate effect on death rates. Birth rates are affected only with considerable lag. Once the crude death rate is low, further absolute decline is limited; but no such limits are imposed on the crude birth rates. Therefore, modern technology will have early effect of accelerating the rate of growth of population. It is only in the later stages of modern economic growth in a country that it may be accompanied by a falling rate of natural increase, i.e. the excess of births over deaths as a percentage of total population. In the early phases of the use of modern technology to achieve a significant and sustained rise in per capita product is more difficult. For what is then required is not merely an increase in product commensurate with the increase in population, but a much greater rise sufficient to lift the level of per capita income in order to provide a basis for further sustained growth. From the data the timing of the acceleration in growth of per capita income relative to that in population cannot be determined. No a priori reasons is possible either. All that we know is that the acceleration in the rate of growth of per capita income begins after that in the rate of natural increase of population.

Reasons for the declining phase in per capita income are difficult to perceive. For example, it is difficult to imagine not only unlimited growth in any social process but equally no inherently compelling reasons for the rate of growth of per capita product

can hardly be viewed as an important factor that will retard the rate of growth. Therefore, retardations in per capita income could at best be explained from the demand side. A long term rise in real income per capita would make leisure an increasingly preferred good. Therefore, one could argue that after a high level of per capita income is attained, the pressure on the demand side for further increases is likely to slacken and hence there would eventually be retardation in the rate of growth of per capita income, but it would come much later than that in the rate of growth of population.

Hence, as mentioned in the second para of this section, the definition of economic growth in terms of the changing pattern of industrial structure is more important, then simply a growth of income in per capita over a period of time. It is more so, in a study of the explanation of modern economic growth which is taken up in the next section.

Check Your Progress 3

- 1) What are the two ways in which the changes in industrial structure due to economic growth?

.....
.....
.....
.....
.....
.....
.....
.....

- 2) What is the difference in a) the share of agricultural sector in the national product b) comparative product per worker between manufacturing and services and c) intersectoral inequality in income per worker, between groups of high per capita income countries and groups of low per capita income countries?

.....
.....
.....
.....
.....
.....
.....
.....

- 3) Give reasons for the decline in the share of agriculture in the national product during the course of economic growth.

.....
.....
.....
.....
.....
.....
.....
.....

13.5 MODERN ECONOMIC GROWTH: CHANGES IN INDUSTRIAL STRUCTURE

How industrial structure changes with economic growth can be studied in two ways. First employing some available index of economic growth such as national income per capita, we can, at a given point in time, array the countries by their income per capita, and observe the differences in the industrial structure as given by the occupational structure of labour force and of national income among countries. Statistically, we can find out correlation between income per capita and industrial structure. This would at least suggest what may be expected in most countries in the course of modern economic growth. The second, and more direct, approach is to study the long-term records for each country and ascertain the changes in industrial structure that actually occurred in the course of their economic growth.

Statistical findings on both these approaches are available. Some of the findings are now quite familiar and some are perhaps less known. We first summarise these findings.

13.5.1 Statistical Evidence

- a) As we move from groups of countries with high per capita income to those with low, the share of the agriculture sector in the labour force increases, while the share of the manufacturing and the services sector decreases. And the positive association between per capita product and the share of the service sector characterises each of its subdivision i.e. Transport and communication (T), Trade, Banking and Finance (C) and other services.
- b) The widest range is found in the share of the agriculture sector : more than 1 to 4. That in the share of the manufacturing sector is narrower: less than 1 to 3. The narrowest range is the share of the service sector less than 1 to 2. Within the service sector, it is the other services component which includes service activities ranging from professional, personal and business to government, that is responsible for the narrow range of differences. Its share also shows the least regular association with per capita income. These differences are generally variations in responsiveness of the shares of various sectors in the labour force to per capita income. Thus they possibly reflect the response of these shares to the rise in per capita income in the process of modern economic growth.
- c) The share of the agriculture sector in national product is also negatively correlated with income per capita. It is low in countries with high per capita income and high in countries with low per capita income. Also as in the labour force, the share of the manufacturing and service sectors in national product are positively associated with income per capita.
- d) Unlike the shares of the trade and banking and finance and other services divisions in the labour force, which show distinct positive association with per capita income, their shares in national product are about the same in high and in low income countries. The positive association between the share of the total services sector in national product and per capita income is, therefore, chiefly accounted for by the movement of the share of the transport and the communication division whose pattern of association with per capita income is very much like that of the share of the manufacturing sector.
- e) Relative product per worker in the agriculture sector is below 1.0 in most countries, i.e. lower than countrywide product per worker: and that in all groups it is lower product per worker in the non-agricultural sectors combined. What is even more interesting, the relative disparity in product per worker between the agriculture sector and the non-agricultural sectors tends to be wider in the low income than in the higher income countries. The underdeveloped countries are further behind the developed countries in product per worker in agriculture than they are in product per worker in the non-agricultural sectors.
- f) Product per worker is usually higher in service than in the manufacturing. Furthermore, the difference between the service and manufacturing sectors in product per worker is narrowest in the high income developed countries, and

- g) The transport, communication and trade, Banking and Finance division of the service sector is characterised by generally higher levels of product per worker than the other services division, and here again the relative excess is inversely related to income per capita-being lowest in the high income, developed countries and highest in the low income underdeveloped countries.
- h) Intersectoral inequality in income per worker is narrowest in the high income, developed countries and rather wide in the low income, underdeveloped countries.

13.5.2 Changes in the various Sectors during Economic Growth

The statistical findings based on the examination of the long-term trends reveal that with minor variation most of the trends observed in a cross-section survey are born out: Economic growth is generally associated with a decline in the share of the agriculture sector both in labour force and income. The share of the manufacturing sector shows a rise in both labour force and national product. However, the rise in the share of the labour force is generally not as large as was observed in a cross section study of economic growth, long term trends also show a rise in the share of the service sector in the labour force, but its share in national product does not give any consistent movement.

In most countries a rise in income per worker in the agriculture sector, relative to that in the non-agricultural sectors is observed. This means that the rise in per worker product in the agriculture sector has been even greater than that of the non-agricultural sector. Furthermore, within the on-agricultural part of the economy, the rise in the per worker product in the services sector was more moderate than that in either the manufacturing or the agricultural sector. In respect to the movements of sectoral levels of income per worker, the trends shown by the long-term records are consistent with what we could expect from the cross-section analysis.

13.5.3 Trends Explained

The findings summarised in the previous section and the more detailed evidence available elsewhere needs an explanation. The first relate to the finding that there is a shift away from agriculture during the course of economic growth. Without dealing thoroughly with the wide complex of trends involved and factors underlying them, one may well ask what major forces are there which lead to such a shift. The second is the less familiar finding. This relates to the narrow range of differences in the shares of the service sector in labour force and national income in both types of countries and the corresponding diversity of trends over time in the share of the service sector in the national income. The third is the reasons for, and implications of, the much wider intersectoral inequality in per worker product in under-developed than in developed countries. The explanation of these three findings is given below:

a) Decline in the share of the Agriculture Sector due to Engel's Law

The decline in the share of the agriculture sector in labour force and national income has a customary explanation. It is found in the application of the Engel law to processes of income change over time. If real income per worker and hence per capita increases, the demand for products of sectors other than agriculture is likely to rise more than the demand for the products of agriculture. People with higher income spend proportionately less on food as compared to people with low incomes. Hence, in a closed economy, a rise in per capita real income will be accompanied by shifts in the structure of total output from the agriculture sector. This would be true in an open economy also. The shift of total demand will favour a greater share of domestic output for the non-agriculture sectors. Therefore, if the demand shifts away from the agriculture sector, the share of the latter in real income will decline, and so will its share in the labour force unless productivity per unit of labour falls which is unlikely.

b) Rise in Productivity in agriculture as a pre-condition for industrialisation

There is, however, another link to this argument also. It has to be with the condition for the rise in product per worker, and hence in per capita product. It is a pre-condition of industrialisation that productivity of labour in agriculture increases sufficiently to feed, at higher per capita levels, a larger proportion of

that in most of the developed countries, product per worker in the agriculture sector increased more than product per worker in the rest of the economy combined. Therefore, one may claim that a marked rise in productivity per worker in agriculture is pre-condition of the industrial revolution for any sizable region in the world. Moreover, any country in which the product per worker in the agriculture sector is low will tie to the land, at low income levels, a large part of the population. Such countries will have little margin for the non-agricultural sector to grow upon. On the other hand, when modern economic growth does occur, it is the combination of the marked rise in productivity of labour in the agriculture sector, with secular limits on the demand for its product that results in such a sharp and uniform reduction of the agriculture sector in the labour force.

13.5.4 Narrow Range of Differences in the Shares of the Service Section in two types of Courses

Several reasons may be adduced to explain the narrow range of differences in the share of the services sector associated with differences in per capita income. First, the products of the service sector are less easily imported and exported than are the commodity products of the agriculture and manufacturing sectors. Some services are, however, embodied in values of commodities, and can easily be exported or imported. But many others: government, professional, personal, retail distribution, and similar services—cannot move across a country's boundaries. The international division of labour thus permits a country to concentrate on either the agriculture or the manufacturing sector, but not to dispense with a sizable minimum of service sector goods that must be produced at home.

Second, the service sector includes a wide variety of miscellaneous activities, some of which may be in larger supply in low income countries than in high and vice-versa. For example, domestic and personal services, religious services, and the like are in larger supply in under-developed countries while the professional, educational, and business services, are in large supply in high income countries.

A third and related factor bears particularly upon the share in the labour force. The pressure of population on land and an increase in the productivity in agriculture in the less developed countries may mean a movement of the surplus labour in agriculture into service activities. Firstly, because some of the services demand little capital and yet provide some modicum of living. For example, peddling, cart transport and personal services of various descriptions. Secondly, the employment of this surplus in the manufacturing sector is inhibited partly by capital scarcity and partly by competition of the manufacturing sector in the more developed countries.

A fourth factor is of particular bearing upon the share of the service sector in national income, we have seen that despite the inclusion of large groups of low-paid activities, the average income per worker in the service sector in the under-developed countries is higher relative to that of the per-worker-income in other sectors, than in the developed countries. This is due to the extremely high relative income of some groups within the service sector of the under-developed countries.

Thus given the heterogeneity of the services sector, and the difficulty in moving its goods across a country's boundaries, it may be that economic growth is not necessarily accompanied through all phases by a rise in the share of the services sector in either labour force or national income. But we have seen that the share in the labour force tends to rise fairly generally. This requires explanation. Why should the growth of an economy be accompanied by such a consistent shift of labour into service activities?

The explanation lies in the increase of productivity in the agriculture and manufacturing sectors. In general, this increase is attained, particularly in the manufacturing sector, by concentration of production in large-scale units. Such concentration in scale and continuity in time require a large volume of ancillary services- transportation, communication, distribution, etc. Furthermore, increasing urbanisation calls for increased government services. The demand for an educated population and labour force increases service activities in education. The generally

greater complexity of the economic system requires more supervision by government in the way of legislation, regulation and administration. Thus, over and above any shift in demand by ultimate consumers in favour of services that may occur with a rise in real income per capita, there is perhaps the more important rise in the demand for service activities as a necessary complement to the concentrated and specialised high-level productivity organisation in the agriculture and manufacturing sectors. Given greater demand for the products of the service sector, and a somewhat lesser increase in per worker productivity in many divisions of this sector than in the agriculture and manufacturing sectors, the shift in the labour force toward high proportions in the service sector is easily explained.

13.6 INTER-SECTORAL INEQUALITIES DURING MODERN ECONOMIC GROWTH IN DCs AND LDCs

In the low income, underdeveloped countries, despite the fact that the services includes larger proportions than elsewhere of extremely low-paid occupations, the product per worker for the sector as a whole is appreciably higher than in the other parts of the economy. This means necessarily that in some divisions of the services sector product per worker (including entrepreneurs) must be extremely high relative to the countrywide product per worker. This is true in the commerce division (trade, banking, etc.) and in the professional and government sub-divisions.

13.6.1 Reasons for Higher Labour Productivity in Services Sector

There are two major reasons why product per worker in these selected divisions of the services sector is so much higher relative to the countrywide average in the less developed countries (LDC) than in the more developed countries (DCs). First, the commerce division in the less developed countries is generally dominated by traders, landlords, and money lenders who constitute a group of entrepreneurs. Under conditions of capital scarcity and economically weak position of the large masses of agricultural cultivators, small handicrafts men and shopkeepers these entrepreneurs enjoy a monopoly position and a great economic advantage that may secure for them returns which may absolutely smaller per head than those in the developed countries but are a much larger multiple of the per worker income for the country as a whole. No such monopoly advantages and superior economic power attach to similar group in the better-organised advanced economies of the developed countries.

Second, among certain occupations in the services sector, particularly the professional, minimum levels of income are required for the adequate pursuit of activity, and these minimum levels are a larger multiple of the country-wide income per capita or per worker in the less developed than in the more developed countries. Since the services sector of the less developed countries includes large groups whose occupation requires substantial minimum levels of absolute income per capita, the very low level of the country-wide income per capita, or per worker means that these groups are quite high in the array by relative income position within the country. Furthermore, the connection between the scarcity advantages of occupations requiring a substantial capital investment in education and training and the high levels of their relative income position is much closer in the under developed than in the developed countries.

It follows that in the process of economic growth the increasing supply of capital, both for material investment and for investment in human beings, means a substantial reduction in the factors just adduced to explain why certain groups within the services sector in the underdeveloped countries secure per worker incomes so much higher than the countrywide average. The increased employment opportunities for large groups of the population, at places in the economy where they can be provided with substantial capital per head, mean a greater rise in the per worker product in

13.6.2 Inequality in the size-Distribution of Income

The wide intersectoral inequality in product per worker in the less developed countries suggests that general inequality in the distribution of income by size in these countries may also be quite wide, perhaps wider than in the developed countries. If the countrywide real income per capita is low, the effects of inequality on the welfare position of the masses of the population whose income is significantly below the average are far more serious in terms of material deprivation than in countries where the average income is higher. To be sure one cannot pass simply and directly from measures of product per worker originating in the various sectors to differences in income received by various groups within the population: income originating includes returns on a assets which do not necessarily accrue to the members of the labour force attached to a given sector. But in all countries compensation of employees and entrepreneurial incomes account for by far the largest proportion of total income originating (or of net product turned out) the ratios usually being about 80 per cent. The proportions of total product that are not distributed (retained as corporate savings or government profits) or are distributed to the small group of pure rentiers usually do not amount to more than a few percentage points of national product. Therefore, the intersectoral inequality in product per worker is highly suggestive of inequality in the distribution of income by size among the individuals and households who comprise a country's population. If this is true, the inference that inequality in the size distribution of income is possibly wider in the under-developed than in the developed areas, and the conclusion that such inequality is reduced in the course of economic growth as suggested by the narrowing of intersectoral inequality in product per worker are both plausible.

Check Your Progress 4

- 1) Mention the two main reasons which product per worker in same selected divisions of the services sector is higher than nationwide average in the LDCs than in the DCs.
.....
.....
.....
.....
.....
.....
- 2) What are the reasons for the inequality in distribution of income by size in developing countries.
.....
.....
.....
.....
.....
.....
- 3) Describe the trends in the distributions of income by factor shares and in the size distribution of income.
.....
.....
.....
.....
.....
.....

13.7 MODERN ECONOMIC GROWTH: OTHER TRENDS IN THE ECONOMIC STRUCTURE

In the previous section, we have seen modern economic growth as a phase characterised by rapid shifts in the industrial structure of product and consequently by rapid shifts in the share of labour attached to various sectors in the economy. If we classify economic units by size and type, then further analysis of modern economic growth can be facilitated by a further analysis of distribution of product, and also allocation of labour among economic units classified according to type and size. For example movement away from agriculture was associated with marked reduction in the share of small own account enterprises in aggregate output and of industrial entrepreneurs and own account workers in the labour force. The intersectoral shifts were also accompanied by growth in the scale of firms and changes in the type of organisation within sectors. For example, in the manufacturing and the trade sector small incorporated firms gave rise to large corporate units.

13.7.1 Changes in Distributional Aspects

The shifts in industrial and type of firm structure of national product and the associated allocation of labour force were quite marked and rapid. However, similar trends in other aspects of economic structure were rather missing or were very moderate.

This was more true in what we may call the distributional aspects of economic structure. For example in the trends of the distribution of income both by factor shares as well as in terms of size distribution of income, relatively mild shifts were observed in developed countries which indicate narrowing of inequalities in these countries in the personal distribution of income.

Similarly, very moderate trends were observed in the allocation of product by use particularly between capital formation and consumption. The gross national capital formation proportions rose from about 10 per cent to 20 per cent and the net from 5 per cent or less to between 10 per cent to 15 per cent. Despite the enormous rise in reproducible capital stock per capita per worker consumption continued to account for the overwhelming proportion of gross and net national product, though the nature of consumption changed according to the changes in industrial structure.

13.7.2 Three Other trends in Modern Economic Growth

Besides the internal structure, modern economic growth was characterised by three other prominent trends. Firstly, the technological revolution in transport and communication facilitated contact among various parts of the world. Secondly, modern economic growth spread sequentially from its pioneer beginning in 18th Century England to various follower countries with the timing of entry continuing even today. Thirdly, until the entry of Japan in the late 19th Century followed by USSR in 1930s modern economic growth was concentrated in European countries and their offshoot overseas, whose per capita income were quite high even before industrialisation and certainly much higher than the incomes of countries in Asia and Africa.

These three-features alongwith the high rates of aggregate growth and the shifts in the internal structure led to a variety of associated trends in the internal structure led to a variety of associated trends in the international aspects of modern economic growth process among the developed countries and in their relation to the underdeveloped part of the world. These trends are seen in the international flows of men, goods and capital.

13.7.3 International Flows of Men's Good and Capital

The international flows of men, goods and capital were at high rates from the second quarter of the 19th century to World War I. The migration stream were particularly important for the overseas offshoots of Europe such as North America, Oceania and

product rose significantly from 1820 to World War I both in developed countries and the steadily increasing number of UDC drawn into the network of World trade. With minor exceptions upto 1913 a law of increasing share of foreign trade in aggregate product seemed to have operated. Foreign capital investment flows also grew rapidly from the second quarter of the 19th century to World War I.

However, with World War I came a radical change in all the three flows. The effect on international migration was particularly marked and it never recovered to levels of the pre World War I proportions. Almost similar distinguishing effect was noticed in economically oriented international flows of capital funds, i.e. excluding politically motivated grants and donations. Despite continued major improvements in transportation and communication, proportion of foreign trade to aggregate output barely returned to the levels attained on the eve of World War I.

These trends apparently seemed to be the result of the sequential spread, the high rates of aggregate growth and the rapid shifts in internal structure. **The sequential spread** rather than simultaneous emergence meant inequalities in the rate of aggregate growth even among the countries that eventually became developed let alone between all of these and the underdeveloped areas of the world. The high rates of aggregate growth meant that the absolute differences of growth rates even among developed countries were wide and, therefore, commulated rapidly into marked shifts in relative economic and political power among nations.

Check Your Progress 5

- 1) Why did modern economic growth originate in England?

.....
.....
.....
.....
.....
.....
.....
.....
.....
.....
.....

- 2) Do you agree that the spread of modern economic growth has been limited?

.....
.....
.....
.....
.....

- 3) What are factors on which the length of the transition period between revolutionary break through and the reaching of threshold depend?

.....
.....
.....
.....
.....

13.8 SPREAD OF MODERN ECONOMIC GROWTH

revolution which provided the base for modern economic growth originated in a small country—Great Britain in the 1780s. This country at that time accounted for only slightly over 1 per cent of the total world population. We have also mentioned that this revolution instead of simultaneously occurring in the other countries within the European framework, which had large populations and were better organised than Great Britain, was confined to Great Britain for some decades before it spread to other countries. In the course of our discussions of the rates of growth and changes in the internal structure of economies experiencing modern economic growth, we had also indicated that even after a lapse of almost one and three quarters of a century modern economic growth could reach only about one-third of the total world population. Therefore, the natural question that needs to be answered in the context of the spread of modern economic growth is to show if the rate of spread was limited and if so, why?

13.8.1 Was the Spread of Modern Economic Growth Limited?

When we say that the rate of spread is limited, this is not to deny that some elements of modern economic growth have not affected all corners of the globe. What we mean by this statement is that the spread effect has not been enough everywhere—where economic performance in the aggregate has led to a thorough transformation of a country's economic and social framework. For example we cannot say that modern economic growth has not affected India or for that matter countries in Asia and Africa. But it is a common knowledge that majority of the countries in these regions are still termed as developing.

The question of low rate of spread can be answered if we can show that (i) the pioneering impact of modern economic growth had restricted locus; (ii) the length of the transition period was large which contributed to the slowness of the spread and (iii) the gap between developed and developing countries is widening and is riddled with increasing difficulties. These, are however, questions to which only speculative answers are possible. Nonetheless there are important as only through answers to these questions we can shed light on our main question.

13.8.2 Why did Modern Economic Growth Originate in England?

The question that industrial revolution could have originated only in England is explained with the help of various theories. Chief among them are those that seek to explain the phenomenon in terms of (a) climate, geography and biological factors; (b) historic accidents and (c) through only political factors. Although no one can deny the importance of these factors as explaining the industrial evolution originating in England, these are, however, by no means complete explanations. We shall show that the main pre-conditions for industrialisation were already present in eighteenth century Britain, but what gave it superiority over other countries was that the political and social framework was favourable to vigorous entrepreneurial drives aimed at technological and economic innovation.

England in 18th century was certainly not under-developed by the standards generally applied to the underdeveloped countries of today. By 1780 England did not have subsistence agriculture and hence there were no major obstacles to the transfer of men from non-industrial to industrial pursuits. The country had accumulated and was of sufficient size to permit investment in necessary equipment for economic transformation. Enough of the investable resources were in the hands of men willing to invest in economic progress while relatively little was in the hands of men likely to divert resources to economically less desirable uses. The country possessed an extensive and fairly highly developed manufacturing sector. Transport and communication was fairly easy and cheap. The technological problems of the time were fairly simple. They required no class of men with specialised scientific qualifications; but simply sufficiency of men with ordinary literacy, familiarity with simple mechanical devices and the working of the metal, practical experience and initiative. All this, however, does not mean that there were no obstacles in the path of industrialisation, but only that they were easy to overcome because the fundamental social and economic conditions for it were already present. Great Britain in this sense was a unique case, unmatched by any other European country of the day. If the situation was as indicated above, the industrial revolution could not have occurred concurrently in other countries in Europe, let alone in the rest of the

Secondly, there were in England inherent compulsions to respond to the major bottlenecks that were emerging within the economic technology of the time. The constraints imposed by the old economic technology were more acute and had reached its limits. For example, while England with its scanty forests and deep mines was under pressure to find a source of fuel and power, Sweden with its abundance of woods, and for that matter Netherlands, which had no wood, coal or iron, faced no such problem. Moreover, it is possible to conceive that such technological opportunities are not likely to be equally available to all countries equipped to exploit them if they are a matter of natural resources, or geographical location or other unequally distributed endowments. Therefore, the beginning of such technological revolutions are likely to have a narrow locus.

So far we have shown that industrial revolution could not have its origin in any other country than England. We now take up the question why it could spread to only a very small proportion of the world population in a period extending over one and a quarter of a century? To answer this question we look into the length of the time involved in the spread of new technology within England to a point where it began to exercise a widely transferring effect on the economy and in the adoption of new technology and the associated institutions by the follower countries.

13.8.3 The Transition Period in the Spread

The length of the transition period from the revolutionary break-through to the time that the threshold is reached depends partly upon the nature of the epochal innovation, partly upon the capacity of the pioneer country or countries to exploit the new opportunities at a high and sustained rate and partly upon the extent of communication and shared antecedents between the pioneer and other would be follower countries.

Historically it is impossible to pinpoint the date at which the outline of the revolutionary transformation of technology and the associated changes in society and economy became apparent. Some of the known facts, however, tell us that:

- a) The cumulative effects of the revolutionary technologies in England became evident several decades after 1780s when major innovations associated with the industrial revolution had all been introduced and proved feasible.
- b) The spread of iron (later steel) as the basic industrial material and of steam as a source of industrial power took a number of decades, requiring the development of machines for processing metals, as well as several major innovations to extend the use of steam from stationary purposes to its application in transportation, first in inland waters, then to land and finally in the mid nineteenth century to the oceans.

13.8.4 The 'Follower' Countries

Having considered the time span between the beginnings of modern economic growth and the date at which the process of spread may reasonably be expected to begin, we turn to the process of spread itself. For this purpose the follower countries can be distinguished by their distance both geographical and historical and then one may observe the timings of the necessary political and other institutional changes conducive to technological adaptations that were brought about in these countries. This will help in the understanding of how the process of spread got under way for we have seen that for any technological innovation to bear fruit in term of production, society's attitude to such changes must be positive.

If we begin with Western European countries, which shared with Great Britain a long stretch of common history, a number of similar institutions, views and values, we find that in these countries several major institutional and political changes were made either before or during the transition to modern economic growth. But major structural changes cannot proceed at high speed without threatening the unity of a country. Therefore, even among the European countries, nearest and most closely allied historically to pioneering Great Britain, entry into modern economic growth got delayed, until major required political and institutional changes were brought about.

Similarly observations can be made concerning the societies descendents of Western European countries overseas. For example, in USA, the development of the political framework could mature after some decades of its independence. The distinctive transition to modern industrialisation did not begin in the United States until the late 1830s. In other countries, the delay in the formation of an adequate political structure also meant in turn a delay in possible participation in modern economic growth. For example, far reaching political changes could be observed in Australia, Newzealand and Canada between 1850s and 1870 only. It is clear evidence that despite presumably favourable resource supplies, the conditions for effective participation in modern economic growth were not present until well into the second half of the nineteenth century. The delay in establishing a viable political framework was even longer in the case of Argentina (a country with a population overwhelmingly of European stock) despite attainment of political independence early in the nineteenth century.

The conditions in other areas with populations that were overwhelmingly native, inheritors of long distinctive histories, and isolated from Europe, were more pregnant with difficulties and delays. In Africa and some parts of Asia, many of the native societies were not reached by the colonizers from advanced Western powers until later in the nineteenth century. This was partly for technological and partly for political reasons. As a result the economic modernisation in these areas was slow and often late. The effective spread of modern economic growth to these areas began only around middle of the 20th century. In the politically independent countries in Latin America and Africa with large but still traditionally oriented societies, the task of integrating these societies in a widespread and effective process of economic growth was delayed by the political and institutional framework, existing in these societies.

The large states in Asia that remained politically independent particularly China and Japan, are, however, interesting. Aggressive expansion by the developed Western countries in this direction was delayed in part by technological deficiencies of transportation. This explains why significant use of force was not made until the first Opium war with China in 1842 and the Opening of Japan in 1850s. These dates are three quarters of a century after the initiation of modern economic growth in Great Britain.

Japan responded rather promptly by reshaping its institutions and entered the process in the 1870s, while China was continuously beset with difficulties in attempting to make the needed structural changes, and consequently its entry in modern economic growth was delayed at least a hundred years.

These are then some of the observations which points unmistakably as to why spread of modern economic growth was limited and slow. The one and three quarter centuries that have elapsed since the Industrial Revolution, at first, seems to be a long period within which such spread could have occurred. But the period becomes all too short if we allow for the time required (1) to bring the revolutionary beginnings to fruition as a new epochal transformation (2) to adjust the ingerited political and social framework, even in European countries and among European descendants (3) to improve the technology of transport and communication that permits the adequate flow of people as well as the expansion by the advanced countries, primarily European, to the previously isolated and economically underdeveloped countries in Asia and Africa, and (4) to bring about a change from the prolonged colonial status of many of these countries. Therefore its hardly surprising and more so if we take into account the observations on the widening gap between the two types of countries: as given below that modern economic growth spread to only a very small proportion of the world populations.

The common procedure followed to draw a dividing line between developed and underdeveloped countries has been to set a minimum per capita. The entire analysis then is carried out by analysing if the minimum level of the per unit product of a developed country has risen over the period simultaneously with the growth potential provided by modern technology; and how much of this rise has exceeded the rise in per capita income or per worker product of underdeveloped countries and thus widened the gap between this product and the minimum line of development: The

the minimum per capita. There are enumerable problems in defining that minimum. Without going into these difficulties in detail we answer this question using one alternative framework.

13.8.5 An Alternative Framework for Analysing the Spread

If we define the spread of modern economic growth as the capacity to satisfy some end goals that can be attained by successful exploitation of the potential provided by modern technology we can distinguish between aspiration towards it and its realisation. Some indirect evidence of the gap between the two can then be deduced. Because of the tremendous advance in transportation and communication and the influence of demonstration effects, aspirations have spread much faster than realisation. While aspirations may have always outpaced realisation in all countries, developed and underdeveloped, but the recent increased exposure of the under developed countries to the more advanced countries and their closer contacts have probably produced a wide gap between aspiration and realisation than existed in the presently developed countries in earlier times. Although we have no evidence to support it, it seems plausible.

13.9 LET US SUM UP

In this unit we have discussed characteristics of modern economic growth. After defining the term modern economic growth we have shown that high rates of growth, rapid shifts in the industrial structure of product and labour force, in the distribution of aggregate product and allocation of labour force among economic units classified by size and type, changes in the distribution of income both by factor incomes and size of households, changes in the allocation of product use—between capital formation and consumption and changes in the international flow of men, goods and capital have been the common characteristics shared by all developed countries. We have also shown (a) how relations largely among these countries but also between them and others led to the spread of modern economic growth; and (b) the common characteristics are inter-related and that the association between the aggregative and internal structure characteristics and the character of its spread and the effects on international relations all stem from a common source called technological revolution. The increased power of technology applied to international transport and communication carried across national boundaries the consequences of rapid shifts in the internal structure of developed nations. It also contributed to the sequential spread because the institutional changes required to provide the proper auspices for economic modernisation are so radical that simultaneous emergence is difficult. The trends observed in the economic structure of developed countries seem to be the result of sequential spread, the high rates of aggregate growth and rapid shifts in the internal structure. The sequential spread rather than simultaneous emergence would mean inequalities in the rates of aggregate developed let alone between all of these and the underdeveloped areas of the world. The high rates of growth would mean that the absolute differences in growth rates among developed countries would be wide and would cumulate rapidly into marked shifts in relative economic and political power among nations. This is what precisely had happened.

We looked at the reasons why Modern Economic Growth originated in England and discussed whether the spread was limited. We also described the coming of modern economic growth in the follower countries.

13.10 KEY WORDS

Per Worker Products : Total product divided by the number of workers.

Innovation : Invention of product or process which has been put to productive, often commercial, use.

Epoch : A particular historical period set off from others on the basis of distinctive characteristics and features.

13.11 SOME USEFUL BOOKS

Hobsbawm, Eric, *Industry and Empire*, Pelican, London

Kuznets, Simon, 1966, *Modern Economic Growth: Rate, Structure, and Spread*, Oxford and IBH Publishing Company, New Delhi.

13.12 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) Hint: read section 13.2.1 in the text and answer
- 2) Hint: read section 13.2.2 in the text and answer
- 3) Hint: read section 13.3.1 in the text and answer

Check Your Progress 2

- 1) Hint: read section 13.4.1 in the text and answer
- 2) Hint: read section 13.4.5 in the text and answer
- 3) Hint: read section 13.4.4 in the text and answer

Check Your Progress 3

- 1) Hint: read the introductory paragraphs of section 13.5 in the text and answer.
- 2) Hint: read section 13.5.1 in the text and answer
- 3) Hint: read section 13.5.3 in the text and answer

Check Your Progress 4

- 1) Hint: read section 13.6.1 in the text and answer
- 2) Hint: read section 13.6.2 in the text and answer
- 3) Hint: read section 13.7.1 in the text and answer

Check Your Progress 5

- 1) Hint: read section 13.8.2 in the text and answer
- 2) Hint: read section 13.8.1 in the text and answer
- 3) Hint: read section 13.8.3 in the text and answer

UNIT 14 APPROACHES TO STAGES OF DEVELOPMENT

Structure

- 14.0 Objectives
- 14.1 Introduction
- 14.2 Marxian Theory of the Social Production Process
 - 14.2.1 Forces of Production
 - 14.2.2 Relations of Production
 - 14.2.3 Social Surplus and Class Relations
 - 14.2.4 Mode of Production and Superstructure
- 14.3 Marxian Analysis of the stages of Development
 - 14.3.1 Primitive Communism
 - 14.3.2 Ancient Slavery
 - 14.3.3 Feudalism
 - 14.3.4 Capitalism
 - 14.3.5 Socialism/Communism
 - 14.3.6 The Asiatic Mode of Productions
 - 14.3.7 Certain Questions Regarding the Marxian Stages
- 14.4 The German Historical School
 - 14.4.1 Friedrich List
 - 14.4.2 Bruno Hildebrand
 - 14.4.3 Karl Bucher
 - 14.4.4 Werner Sombart
 - 14.4.5 Hoselitz's views on the German Historical School
- 14.5 Rostow's Analysis of the stages of Development
 - 14.5.1 The Traditional Society
 - 14.5.2 Pre-conditions for take-off
 - 14.5.3 The Take-off
 - 14.5.4 The Drive to Maturity
 - 14.5.5 The age of High Mass Consumption
 - 14.5.6 An evaluation of Rostow's Stages of Growth
- 14.6 Gerschenkron's Theory of the Stages of Development
 - 14.6.1 Gerschenkron's Propositions
 - 14.6.2 The Role of Institutions
 - 14.6.3 The "stages" in Gerschenkron's Approach
- 14.7 Let Us Sum Up
- 14.8 Key Words
- 14.9 Some Useful Books
- 14.10 Answers to Check Your Progress Exercises

14.0 OBJECTIVES

This unit aims at presenting and discussing some theories which see economic development as taking place over stages that is, the theories that are stages-of-growth theories. After going through the units you should be able to:

- analyse the nature and concept of a stage in development
- describe and discuss several stages-of-development theories.

14.1 INTRODUCTION

You are familiar with the concept of development. Among various theories which seek to describe and explain development, are several which see the process of economic development as a series of transition from one stage to another. This unit studies some of these theories of 'stages-of-development'. We shall be using the terms stages-of-growth and stages-of-development interchangeably.

What is a stage of development? Is it merely an analytical construct, that is, a part of the theorists' tool-kit, to comprehend a socio-economic historical process? Or is it a descriptive historical category, that is, is it a unique independent historical item which can be studied? In other words, is a 'stage' a tool or a method with which to study a

seems to be little unanimity in the answers to these questions, or even in the definition of a stage of development itself. Thinkers also disagree on whether these stages only offer theories on the forms of economic organisations in the process of economic and social development or whether they are conceived with the inner logic of evolution and the process of change of the social structure.

There are other fundamental questions regarding the scope, rationale or the very validity of viewing economic progress in terms of stages. Are there stages present in every case of development? Does every country or society go through the same stages? Can some stages be skipped? Do the stages follow each other in the same sequence? Can a society, come back to an earlier stage from a subsequent stage? In other words, can the process be reversed? What are the factors bringing about changes from one stage to another? Since the exact meaning or definition of stages is not unanimously agreed upon, we shall not provide a formal definition. Suffice it to say that a theory of stages basically puts into several unique and distinct periods the historical evolution of a social system or of a particular phase of development process.

In this unit we shall discuss several theories about the stages of development: the Marxian theory, the German Historical School, Rostow's theory and Gerschenkron's theory.

14.2 MARXIAN THEORY OF THE SOCIAL PRODUCTION PROCESS

Marx began with a simple point: in order for human societies to survive, evolve and develop people must produce goods and services. Production is the essence of the existence and development of societies. In order to produce, human beings act to influence, adopt and control nature. Production is of course, not an individual act—it is social in nature (even Robinson Crusoe had his Man Friday!). Logically, therefore, social production has two aspects: one, which characterises Man's relation with nature and the other, the relations amongst men in the production process.

To understand Marxian theory about the stages of development, it is necessary to be clear about certain concepts and ideas Marx has used to explain his theories. We turn to these now.

14.2.1 Forces of Production

Any form of production involves three things: some natural resources, implements of some sort and human labour. Even in the simplest forms of production, people are acting upon natural resources of some kind or other with the help of implements or machines, and their own labour, sweat and toil. Examples of natural resources land, minerals, metals and so on. Marx called these **objects of labour**. Upon these objects of labour people use and apply implements, which Marx denoted **instruments or means of labour**. Instruments of labour can be of the simplest kinds like hammers, shovels, or spades. Or they can be advanced or complicated machinery like heavy machinery, tractors, machine tools, computers or other instruments. The third aspect in the production—people's own toil—Marx called **labour power**. It is the sum total of Man's effort, talent and latent capabilities to transform nature literally by his own hands.

Of the three elements—objects of labour, instruments of labour and labour power—the first two make up the material basis of production. Marx called this material basis of production, made up of object of labour and instrument of labour, the “means of production”

Thus production is carried out using means of production and labour power. Means of production and labour power together, in Marxian theory is called ‘**forces of production**’. Forces of production reflects the state of Man's relation with nature. You can think of forces as roughly the essence of technology plus the ideas, skills and the productive capacity of labour. More advanced the technology, the higher are the forces of production. Thus, industrial societies have higher forces of production than

tribal societies. You must keep the concept of forces of production well in mind. 'Forces of production' is one of the crucial points in explaining the process of development of societies. Another concept is **relations of production** or **production relations**.

14.2.2 Relations of Production

People work in factories, farms, in offices or in mines. During production process people act on nature, work with instruments. But they also have relation among themselves—as colleagues, as bosses and subordinates as employer-employees and in many other ways. Everywhere production is social and people interact, hence, relations take shape. The sum total of social relations that human beings establish among themselves in the social production process is known as the 'relations of production'. The relations of production is also called the economic base. The relations of production are not limited to the point of production but extends to distribution as well.

14.2.3 Social Surplus and Class Relations

Unless a society is very primitive, production yields some surplus quantities of the products. Surplus product is the production which is over and above what is necessary for the maintenance of the instruments and objects of labour. In simple terms, you can think of it (for the economy as a whole) as the national income or the social product.

From the total product, if we deduct the intermediaries, you get the net value added. This is the surplus product. How the surplus is distributed among people who contribute to the production process is one of the central questions investigated in Marxian theory.

Marx differentiated among various classes on the basis of the relations of production. What is a class? Marx has not given a formal definition but has sought to identify classes depending on where they are placed in the production process. In different writings Marx has given different numbers of classes existing in societies but has broadly identified two broad classes: those that own the means of production and thus appropriate or corner almost entirely the surplus and those who do not own the means of production. Although there may be many classes, Marx held that they tend to coalesce into these two broad groups.

Once you have classes and the unequal distribution of the social surplus you also have exploitation and class struggle. In the Communist Manifesto, written more as a political pamphlet, and before Marx turned to more serious and mature writing on economics and political economy, Marx and Engels said "the history of all hitherto existing societies is the history of class struggles". According to Joseph Schumpeter, class struggle has the same importance in Marxian theory as the 'prince of Denmark' has in Shakespeare's Hamlet.

The immediate objective of a class is material and economic. It is a struggle for division of the social product between the classes who work and produce but are exploited and do not own the means of production, and those who appropriate the surplus social product (the propertied class). The ruling class functions as a ruling class essentially through the appropriation of the surplus product.

14.2.4 Mode of Production and Superstructure

You have seen what means of production are. You also know what the term relations of production or production relations means. Production relations and the means of production together make up a **mode of production**. Each mode of production is a specific combination of forces of production and relations of production so organised that it can sustain a distinctive mode of appropriating surplus. You can think of a mode of production as roughly the economic structure and the sum total of production processes in a society.

The mode of production, which corresponds to a certain level of the forces of

mode of production also determines a certain level of social consciousness. Marx held that people's existence determines their consciousness rather than the other way around. In his famous preface to the '*A Contribution to the Critique of Political Economy*' Marx said, "the mode of production in material life determines the general character of the social, political and spiritual processes of life".

Let us briefly review the relationship between the various concepts discussed. In the production process, objects of labour and means of labour make up the means of production. Means of production and labour power, coupled with knowledge, skills and productive capacities together constitute the forces of production. Forces of production together with the relations of production go to make up the mode of production. The mode of production is the foundation on which is based the legal, political and even spiritual superstructure.

Check Your Progress 1

- 1) Distinguish between means of labour and objects of labour.

.....
.....
.....
.....

- 2) Briefly explain what is meant by the term 'forces of production'.

.....
.....
.....
.....

- 3) "Each mode of production depicts a relationship between the forces of production and the relations of production". Explain briefly.

.....
.....
.....
.....
.....

14.3 MARXIAN ANALYSIS OF THE STAGES OF DEVELOPMENT

Now we are in a position to explain Marx's analysis of development as stages in social progress in terms of the transition from one mode of production to another.

Since the mode of production is composed of the forces of production and the relations of production, there must be a harmonious combination of these for mode of production to exist and sustain itself. Minor changes may go on within the mode of production all the time but these do not lead to a change of the mode of production.

There comes a time in the history of every mode of production where the forces of production develop to such an extent that there is disharmony between the forces of production and the relations of production. Then the existing relations of production become a hindrance, a barrier or as Marx put it, 'act as fetters' to further advancement of the forces of production. Then a revolutionary situation develops. This is expressed in terms of social conflict where class struggle heightens and the resultant social expansion leads to a transition to a new and more progressive mode of production. There takes place a new unity and correspondence between the relations of production and the productive forces. Thus the emergence of capitalism

forces of production. But it also led to the emergence of a new ruling class—the middle class or the bourgeoisie which replaced the merchants and guilders and the aristocratic classes in feudalism and mercantilism.

The history of human civilisation is thus seen in terms of successive stages. Each stage has a distinct mode of production with its own unique features determined by its production relations and forces of production. Every mode of production widely also has its corresponding superstructure. For example, primitive societies may have simple modes of dispensing justice but an advanced capitalistic society will have modern jurisprudence characterised by equality of all before law and well established system of laws and courts.

Before we go on to describe the various stages as put forward by Marx let us briefly touch upon the areas where the changes can come about, in the Marxian scheme. The first area of conflict is **within** the mode of production itself. This conflict is between the forces of production and the relations of production. The second conflict can arise between the mode of production and the superstructure. Although the superstructure is based upon the mode of production sometimes the mode of production may be very advanced but there may be many elements in the superstructure which are remnants or residues of earlier superstructure. For example, a country may be very industrialised but religious practices of earlier ages still persisting.

Now let us get down to describing the various stages or modes of production in the Marxian analysis. There is conflict and class struggle in almost all the stages but the form of these conflict and class struggle varies. Commonly the Marxian analysis has five different modes of production or stages of production:

- a) the stage of primitive communism or the tribal stage;
- b) the stage of the ancient slave system;
- c) the stage of feudalism; and
- d) the stage of socialism/communism.

In addition to these, there is yet another mode of production viz. the Asiatic mode of production, which is found only in some societies and which is not part of the process that leads from one stage to the other of these five modes of production.

These mode of production are not to be taken as a set of definite and exhaustive combination of stages. They are more illustrative rather than definitive in nature. We now describe these stages.

14.3.1 Primitive Communism

The stage of primitive communism has three distinct sub-stages: hunting, nomadic pastoralism and stationary agriculture. The mode of production is characterised by primitive instruments of production and joint (communal) holding of means of production (within the community or tribe) and of the product itself by egalitarian distribution. The level of consumption in this stage is extremely low and there is no surplus production. There are no division on the basis of classes in such a social system.

14.3.2 Ancient Slavery

With the development of the forces of production (i.e. with improved means of production and better acquired knowledge) it was possible to produce some surplus and this provided the material basis for the organisation of private property and made it possible to release some people from material production. Free from the cares of earning their daily living, they were able to devote themselves to the art of ruling (statecraft), philosophy, religion, science and art (the elements of superstructure). A corollary to the origin of property was the first division of the society into classes, into exploiters and exploited, into slave-owners and slaves. This led to the organisation of the slave mode of production. The slave was the property of his master; the latter took away the whole of the product, leaving the slave only the barest minimum for subsistence. The slave, as a result, had no interest in

brake on the development of productive forces the feudal mode of production. However, it was not the case that wherever such transition took place, it happened in a unique predetermined fashion. Marx himself wrote about three different paths of such transition. The essential point is that for any given historical process the transition (or any other transition) can vary widely.

14.3.3 Feudalism

Under feudalism, the landlord class exploited serf labour. Serfs were tied to the land through political and legal mechanisms. They cultivate the land through the payment of feudal ground rent. Because they actually occupied the land and could determine how to work the land, surplus had to be necessarily appropriated through forms of coercion which was non-economic, like social customs and state power. Unlike as in slavery, the serf had the disposal of a part of the product and this gave him some interest in expanding the surplus. However, feudal relations, with the peasants' life-long immobility, retarded further growth of productive forces, and social upheavals paved the way for capitalism.

14.3.4 Capitalism

Capitalism is characterised by commodity production which means the organisation of the economy such that goods, produced in separate establishments, are produced for the primary purpose of sale and purchase on the market. The capitalist, or the owner of these establishments, hires labour power in order to produce. The owner of labour power, i.e., the worker, is no longer tied to the land as in feudalism but is free to sell his labour power. Being freed from the land he is also "freed" of the means of production of which he is deprived in the course of the transition from feudalism to capitalism. While the worker is free, therefore, to sell or not his labour power, he is forced to sell it in order to live, since he is deprived of the ownership of the means of production. Under capitalism, therefore, labour power becomes a commodity that is sold and purchased for a price, which is the remuneration for the worker, or the wage. So while a worker has to sell his labour power to live in spite of the freedom to sell it or not, the capitalist's ownership of the means of production endows him with the power to extract the surplus product called surplus value.

Production for the market, division of labour and production being organised in separate establishments (factories) on the basis of wage labour are the distinguishing features of capitalism. Under this system of production, there are two main antagonistic classes, the capitalist class, which owns the means of production and the proletariat or the workers who, deprived of the means of production, must produce in the capitalists' establishment for survival. The production process is not an end in itself—the capitalist sells the product in the market and appropriates the profit.

In feudalism, extra-economic coercion in the form of state power or religious sanctions was necessary to extract surplus, primarily because the tillers were tied to the soil and production was for the family (or the community). By contrast, in capitalism, labourers being free in the dual sense (free of the means of production and free to supply labour power to any firm) and production being essentially for the market, there was no obvious necessity for such form of extra-economic coercion because, the economic process, i.e. the production and exchange process, bases itself on production and appropriation of surplus value. Economic exploitation of labour power thus comes to the centre stage of capitalist process. However, from this it should not be concluded that the role of extra-economic coercion has been eliminated or even sufficiently reduced under capitalism. Quite to the contrary, such forms of coercion through ideological subjugation and use of state power, directly or indirectly, play a very crucial role in propagation and maintenance of the complex structure of capitalist values, institutions, tendencies and practices.

14.3.5 Socialism/Communism

As regards Socialism/Communism as a mode of production, Marx (or Engels) did not have a 'blue print' of it. However, the thrust of their vision of socialism/communism was that it would be characterised by collective ownership of means of production and would be free of various 'ills' like exploitation of capitalism and other earlier antagonistic modes of production. Their insights have been used to

construct a variety of conceptual types of socialism and communism, as a mode of production as well as a social formation.

Marx and Engels distinguished between a 'lower form' of communism and 'higher form' of communism, or what Lenin called socialism and communism. In the lower form of communism, people are still paid according to their abilities and ownership of the means of production is controlled by the state. In the higher form of communism, the state, as we know it, will wither away and distribution will take place on the principle 'from each according to his abilities, to each according to his needs'.

14.3.6 The Asiatic Mode of Production

The basic feature of the Asiatic Mode of Production is that it had a primarily agricultural economy with small units of production. At the same time, it had a centralised state and bureaucracy. Regulation of water supplies was its primary source of power. Marx postulated this system as operating in Arabia, Iran and India where agriculture was artificially irrigated by canals regulated by the state. The production units were small and scattered and were part of a village system.

14.3.7 Certain Questions Regarding Marxian Stages

Does the Marxian theory of stages propose that all countries have to go through these stages? Is it possible to jump stages, or slide back from one stage to the earlier one? Is it necessary that a society in a stable situation is clearly characterised by a single mode of production (of the ones mentioned above), or is it possible that characteristics of several modes of production can coexist for sufficient periods of time, and even present a symbiotic relationship with one another? Do some modes of production have subtypes like capitalism has had many stages and varieties? These issues, and many other related ones, have generated a lot of debate in Marxian theory. Marx himself talked about how various stages can coexist though at any point of time there will be a dominant mode of production. Further, history shows that such stages can be mixed, or the situation where the dominant mode of production may use the characteristics of other modes to its advantage. Further, the possibility of a counter revolution itself means that we can slide back on stages.

A detailed study of Marx as well as other later marxists and the historical experience of societies indicate that these stages are not to be considered in a definite pre-determined fashion. They are not a system of unilinear causation through history. The central point to grasp in the method of analysis, is that it is a combination of logical and historical methods, which tries to analyse long term social changes and tries to find an inner logic to this dynamics. The method of analysis is not predetermined and closed and perhaps the greatest strength of this method lies in its openness and its ability to incorporate new ideas, structure and facts into its fold.

Check Your Progress 2

- 1) "The ancient slave society did not give any incentive to the direct producers to expand their productive capacities". Do you agree with this statement? Explain its meaning and consequence.
.....
.....
.....
.....
- 2) Why was it necessary to have extra-economic coercion in a feudal society to extract the surplus product? Can you mention some forms of this extra-economic coercion?
.....
.....
.....

- 3) "the proletariat under capitalism is free in two senses". Explain this statement. How is one freedom related to the other? Do these two types of freedom impart progressive character to capitalism?

.....
.....
.....
.....

14.4 THE GENERAL HISTORICAL SCHOOL

The German historical school developed with the rise of nationalism in Germany and as a reaction against English classical economics. They attacked the English school's deductive methods and the formulation of natural laws in economics and held that since the development experience of each country is unique, moulded by its historical circumstances, there cannot be any such natural laws. Their alternative was in comparing the process of development based on actual historical data and then to evolve a theory of pattern of development based on such historical data. They rejected the universal principle of free trade and economic liberalism propagated by the English classical school and argued for interventionist policies based on their understanding of the specific economic situation of Germany.

Apart from their opposition to the English school and the use of historical data in trying to formulate theories and policies, there is very little that is common to the different proponents of the school. We are however not concerned with the general works but the specific contribution they made to the theories of stages of development. Further, as different scholars of the German Historical school and quite divergent opinions on stages of development, we would go into the views of some of the most prominent theorists of the school.

14.4.1 Friedrich List

One of the pioneers of the German Historical School, his main attack on the English school was their lack of interest in deriving generalisations from the study and examination of empirical historical processes. His stages of growth are to be understood in this context. He distinguishes between five stages; a) the savage stage, b) the pastoral stage, c) the agricultural stage, d) the agriculture and manufacturing stage, and e) agricultural, manufacturing and commercial stage.

However Lists's theoretical discussion of economic growth even in slightly explicit form relates only to be a limited portion of his classification. Thus, he is silent about how and why the transition took place between his first three stages. He also did not distinguish between the last two stages. The crux of his theory concentrated upon the transition from the agricultural stage to one on a higher level by introducing manufacture. Even here he ended up with a series of assertion:

- i) that only countries of the temperate zone are suited for manufacture—the rest of the world should produce in agriculture and trade their product with manufacture of temperate countries.
- ii) once a country in the temperate zone has attained a fairly high degree of agricultural development, it can only progress further by introduction of manufactures. This can be done, according to him, in two ways: under free trade, if the nations engaged in trade are in the same degree of progress, and second, by protection of industry through the intervention of the state, if some others have outdistanced the country concerned in manufacture and commerce.

From all this, it seems that List gives importance to only one dynamic element in the process of economic development—the introduction of manufacture. However there is not much attempt even to explain the evolution of stages and in this sense his presentation offers hardly any theory of economic growth. The central point in his writing is to defend German industrialisation, to recognise that such industrialisation

cannot be effectively brought about through free international trade as proposed by Adam Smith and Ricardo of the English classical school (in line with absolute and comparative advantage). Rather, for a late comer to the industrialisation process like Germany there is an initial necessity to introduce protection of the nascent industrial sector. The essential point in theorising in historical categories was to deny the prevalence of universal natural laws—like laws of comparative advantage and free trade. You are familiar with these laws. There was a recognition that the initial historical context specifies the kind of policy which one should adopt for a country and the later stages are targets of progress—that ultimately a country should progress from the agriculture-manufacturing stage to the agricultural-manufacture-commercial stage. Obviously the influence of British industrial progress is clear here. But not of British economics.

14.4.2 Bruno Hildebrand

Hildebrand had an alternative presentation for successive stages of development. He had three stages a) Natural or Barter Economy, b) Money Economy, and c) Credit Economy.

However, these stages can hardly be regarded as complete stages of development—they are at best comparative forms of economic organisation in the sphere of exchange. Further, Hildebrand's theory also suffers from the same lacunae as in List, in the absence of any inner logic of how a society gets transformed from one stage to another, though he postulated the kind of division of labour, social organisation and institutional set up which is possible with each of these stages. Thus, his scheme is also at best a presentation based on empirico-historical observations, and that too related to one particular field of socio-economic organisation—exchange and distribution.

14.4.3 Karl Bucher

The most popular and probably the most widely discussed theory of economic stages in the German Historical School is elaborated by Karl Bucher. Bucher suggests three stages, a) the stage of independent domestic or household economy, b) the stage of town economy, c) the stage of national economy.

There is no exchange in the domestic economy. Production is mainly for the household. Although there is division of labour an institutionalised system of exchange is absent. But certain items of commerce, like weights and measures were present. Exchange is present in the next stage, the town economy.

However, exchange is limited to goods which pass directly from the producer to the consumer, i.e., ideally all production for exchange is customer production. The gradual dissolution of the domestic economy leads to the transition to the town economy.

The stage of national economy is characterised by Bucher as that in which goods are produced wholesale for a market which constitutes the characteristic institution through which they circulate. The producer and consumer are typically unknown to each other, and goods normally pass through many hands before they reach the ultimate consumer. According to Bucher, the transition from the town economy to the national economy is facilitated by the creation of the unified nation state.

What distinguishes Bucher's theory from the earlier ones of the German Historical school is his eye for historical detail in describing and characterising these stages, especially the last two, as well as trying to explain the reasons and the process of transition from one stage to another. The development of the stage of town economy is thus based upon the development of a very special institutional phenomenon, i.e., the development of the medieval Western European city. Again the process of transition from the town economy to the national economy is explained through extra-economic factors like the process of the rise of territorial state organisations and its culmination in the creation of the unified nation state. On the one hand this implies a limitation of Bucher's theory of stages by confining it to an attempted interpretation of the economic growth of Western and Central Europe, but, on the other hand, it also provides a new strength to the theory by explaining the

well studied institutional framework. Bucher's system of stages received widespread acceptance in Europe, essentially because of his description of the essential quality of medieval town economy.

However, there is hardly any casual explanation of the successive transformation based on internal dynamics of the socio-economic system itself, i.e., there is no internal logic inherent in the theory as to how and why such transformation takes place. Thus, while the empirical historical approach of the theory might prove to be an advantage for study of economic anthropology—it has rather limited value as a theory of economic development. Moreover, the fact that Bucher's explanation of the transition as caused by extra-economic factors means the theory has limitations as an explanation of economic growth.

14.4.4 Werner Sombart

The other major work in the German Historical school on stages of growth quite distinct from his predecessors—was by Werner Sombart.

Sombart classifies his stages not on the basis of linear historical periodicity, but on the basis of the degree of social interaction. He calls the three stages a) individual economy, b) transitional economy, and c) social economy.

Individual economy depicts a stage in which social interaction exists primarily within the household and in which only slight contact occurs with other economically active units (an example of this stage is tribal economy or joint family production). The transitional stage is one in which the total needs of the society are met through cooperation of all members of the society, but where the degree of interaction is still limited. In other words, the transitional economy is a mixed stage in which part of these needs are met by individual production of each unit on its own and a part by exchange with others (examples are the medieval manor economy, the village economy, the town economy). Finally, the social economy is a stage in which all needs are met by interaction with others (examples are ancient slave economy, slave economy in modern colonies, capitalist economies, socialist economies).

It is clear therefore that Sombart did not have any linear view of stages in the sense of one stage occurring **after** the other in a sequence—the ancient slave economy occurs in his third stage. The idea of the stages are therefore derived from binding principles of economic systems and not empirico-historical categories. Because the stages were not linear, there was no scope of a theory of linear transition. However, Sombart had a theory of change or dynamism which results in transformation of the economic system from one stage to another (not necessarily linear). Another feature of Sombart's theory is that it does not adequately make clear the concept of the **degree** of social interaction. In what sense does the joint family have lesser social interaction than a capitalist economy. Although there are more individuals involved in the process of interaction under capitalism and these individuals are engaged in more diverse occupations, they are less clearly tied to other members of their society than one economic actor in a primitive economy. The individual in capitalistic economy is more anonymous. However, the ties in primitive economy are based more on social norms and cultural factors than on economic ones.

Apart from interaction, Sombart also brings in differentiation based on economic activity. Production may be carried on for the sake of satisfaction of needs what is, for subsistence or for the sake of acquisition. The first two economic stages are characterised by production for subsistence. The third stage, that of social economy, with the exception of a socialist economy is invariably characterised by the principle of acquisition.

This combination of economic stages and economic principles is derived, at least in spirit, from Marx. There are two aspects of Sombart's theory that merit attention. The first is his insistence on the degree of interaction as shaping the form that economic processes take in a particular stage. The second is his introduction of the concept of motivating economic activity as an important factor influencing the transition of an economy from one stage to another.

The idea of the degree of interaction, determining the stage in which an economy is, implies that any explanation of economic development as a series of stages must regard the stages not merely as forms of economic organisation but rather as forms of social organisation with different economic features.

In stressing the importance of motivation in the shift to a higher stage of development, particularly in explaining the emergence of capitalism Sombart differed from Marx in that he believed that economic consciousness and ideology determine the form of economic organisation rather than the other way around. According to Sombart the same spirit which gave rise to the new state, to reforms in christianity, to the new science and technology also made possible the emergence of capitalism. The blend of what Sombart called the 'bourgeois spirit' and the 'entrepreneurial spirit' made up, according to him the 'capitalist spirit'—the psychological state which facilitated the development of capitalism.

14.4.5 Hoselitz's Views on The German Historical School

The German Historical school emerged as a reaction to the English Classical school. It stressed the use of historical observation in framing generalisations rather than framing economic policies based on uniform natural laws devoid of historical context. Their study of stages of growth is an attempt to understand the historical process of evolution of socio-economic systems.

In an attempt to assess the usefulness of these theories as general theories of stages of growth, Hoselitz points out that if the stages-of-growth theories have to become useful theories to analyze economic development, they must rise above mere historical categorisation. They should try to relate the inner logic of production in each stage and trace the internal dynamics of change so that a theory in the proper sense of the term can be build around it. Obviously this will some of the stages descriptively less accurate but then that is the price one has to pay for theorisation.

Hoselitz held that "In order to be of maximum usefulness for a theory of economic growth, economic stages must be constructed in such a way as to minimise the likelihood that the process of economic change illuminated by these constructs, the merely "possible", rather than the "true", change-generating variables are included. Hoselitz felt that the ideal constructs must be able to mark a main variable (s) which may be made accountable for transition to next stage. Noting the absence of this in the theories developed by the German Historical School, he rejected them as useful "development stages". He felt a theory of stages of social systems is a more useful construct than the theories put forth by German Historical School.

Check Your Progress 3

- 1) What was the broad context of the origin and development of the German Historical School?

.....
.....
.....
.....
.....

- 2) Mention the different stages put forward by a) List b) Hildebrand c) Bucher?

.....
.....
.....
.....
.....
.....
.....

- 3) In what crucial respects did Werner Sombart's view of "stages" differ from the rest of the German Historical School?

.....
.....
.....
.....

14.5 ROSTOW'S ANALYSIS OF THE STAGES OF DEVELOPMENT

Now we turn to the views of W.W. Rostow on the stages of development which is quite a different approach than the previous ones. The earlier theories we have discussed tried to map the entire course of civilisation into distinct stages, where the stage of feudalism or emergence of town, for example, received sufficient attention as did the recent stages of capitalism or national economy. Rostow's main attempt was to evolve a historical approach to industrialisation and further material advance. The pre-industrial period right from the beginning of civilisation has, therefore, not received much attention in his work. He is more concerned with the period just preceding the industrial period—the period of transition where industrialisation take proper roots in his economy—and the age of economic maturity and prosperity hence forth.

A distinctive feature of Rostow's theory is that these stages are not merely descriptive. Rather one stage can be clearly distinguished from another by some crucial socio-economic parameters. Further, on the basis of this, the time period of these stages can be well defined. Let us first know about stages before we come to further comparative evaluation.

The stages are the following : 1) Traditional Society, 2) Pre-conditions for take off, 3) Take off, 4) The Drive to Maturity and 5) The Age of High Mass Consumption.

Rostow points that it is possible to identify all societies in their economic dimensions, as lying within each of these five categories and a society at a particular stage must have passed through the preceding stages.

Let us now have a detailed look at these stages :

14.5.1 The Traditional Society

As Rostow puts it

"A traditional society is one whose structure is developed within limited production functions based on "pre-Newtonian science and technology" and Pre-Newtonian attitudes towards the physical world. Newton here is used as a symbol of watershed in history, when we came widely to believe that the external world is subject to a few knowledgeable laws and was systematically capable of productive manipulation ... The concept of the traditional society is however in no sense static ; and it would not exclude increases in output. But the central fact about the traditional society was that a ceiling existed on the level of attainable output per head".

Rostow recognises "the story of traditional society was a story of endless change"—but the level of productivity was limited by inaccessibility of modern science, its application and its frame of mind.

The two major characteristic of such a society were :

- i) The societies had to devote a high proportion of their resources to agriculture and from this followed a hierarchical social structure with narrow scope for vertical social mobility

- ii) Even if central political rule existed, the centre of gravity of political power generally lay in regions, in the hands of those who owned or controlled lands.

Rostow recognises the limitation of putting diverse set of societies spread across the globe through such a vast period of time in one category—but his aim here is to clear the way for his central subject—the post-traditional society where the major characteristics of the traditional society—its politics, social structure, values and economy were altered fundamentally to permit regular growth.

14.5.2 Pre-Conditions for Take Off

It is, as the name suggests, the stage where the pre-conditions for take-off are present. It takes time to transform the structure, politics and values of a traditional society—so that it is prepared to exploit the fruits of modern science—and grow at an expanded scale. This period of initial transition—where changes in a dynamic sense begin to be visible in the society—is classified in the pre-condition stage. In Rostow's metaphor of an aeroplane, this is the stage where the propeller starts roaring though the air craft still stays stationary. Rostow notes that this stage was initially developed in Western Europe of the late 17th and early 18th century. Britain was the first to develop fully the pre-conditions for take-off. However as a more general case, this stage often arose not indigenously but from some external intrusion by more advanced countries. These invasions shocked the traditional structure and set into motion ideas and institutions which formed the basis by which a modern alternative was constructed. New attitudes to education and knowledge, especially scientific knowledge, developed. Special institutions like banks and other institutions to mobilise capital were formed. Investment increased particularly in transport and communication. The scope of commerce, both internal and external, widened. But all these activities proceeded at a limited pace within an economic and social structure still not completely out of the shackles of the traditional structure and values. The period culminated in the development of the structure of a centralised nation state or a colonial power (or both), a feature which Rostow considers almost a necessary condition for take off.

14.5.3 The Take-Off

We now come to the most important stage in Rostow's classification: the take-off or what he called the great watershed in the life of modern societies. To continue the aeroplane metaphor, this is where the aeroplane takes off, that is, flies off the ground. The take-off is the interval in which the old blocks and resistances to steady growth are finally overcome. The forces of economic progress, which had resulted in bursts and enclaves of modern activity, expand and come to dominate the society and growth becomes a normal condition and not merely an isolated activity.

During the take off, industries expand rapidly, yielding profits that are reinvested, the rate of effective investment and savings will rise from, say, 5 per cent of national income to 10 per cent or more and new techniques spread in both agriculture and industry, revolutionary changes in agricultural productivity being a necessary condition for take off.

The take-off is specifically defined as requiring all three of the following conditions:

- 1) a rise in the rate of productive investment from 5 per cent or less to 10 per cent or more of national income.
- 2) the development of one or more manufacturing sectors, with a high rate of growth.
- 3) the existence or quick emergence of a political, social and institutional framework which exploits the impulses to expansion in the modern sector and the potential external economy effects of the take-off gives to growth an on-going character.

The take-off takes place with certain leading sectors in the economy, where the economy can be divided into primary growth sectors (with high growth-rates due to possibilities of innovation or exploitation of hitherto unexplored sources), complementary growth sectors (where growth occurs in response to advances in the

primary growth sectors) and derived growth sectors (where advance occurs in a fairly steady relation to the growth of national income). The leading sectors at any period of time are thus a limited number of primary sectors, whose expansion yields significant external economy and other secondary effects. In Britain, raw cotton imports and the subsequent setting up of the cotton textile industry constituted the leading sector.

The concept of the take-off was unique in as much that Rostow could identify definite periods in which the conditions of the take-off, being specific quantifiable magnitudes as they were, were fulfilled, in the following manner:

Some Tentative, Approximate Take-off Dates

Country	Take-off	Country	Take-off
Great Britain	1783-1802	Germany	1850-73
France	1830-60	Sweden	1868-90
Belgium	1833-60	Japan	1878-1900
United States	1843-60	Russia	1890-1914
Canada	1896-1914	Argentina	1935
Turkey	1937	India	1952
China	1952		

The Take-off stage is therefore a period when the scale of productive activity reaches a critical level and produces changes which lead to a massive and progressive structural transformation in economies.

14.5.4 The Drive to Maturity

After the take-off there is a long interval of sustained, may be fluctuating progress as the steady-growth economy tries to extend modern technology over the whole front of its economic activity. With some 10 to 20 per cent of national income steadily invested, maturity is attained in about sixty years after take-off. Our aeroplane is fully airborne and is flying at a certain height. At this stage the economy which developed around a relatively narrow spectrum of industries, now extends its range to more refined and technologically more complex processes. Maturity is formally defined by Rostow as the stage in which an economy demonstrates the capacity to move beyond the original industries which powered the take-off and to absorb and apply efficiently over very wide range of resources the fruits of the most advanced modern technology.

14.5.5 The Age of High Mass Consumption

By this stage, the leading sectors in the economy are durable consumer goods and services. This is a stage beyond technical maturity, where societies reach a very high stage of technical progress: by this stage, the welfare state develops. You must be familiar with the concept of the welfare state.

14.5.6 An Evaluation of Rostow's Stages of Growth

Rostow presented a rather mechanical view of history, where all countries must pass through these linear stages in their path of development. In fact the theory almost suggested a prescription for the developing countries in terms of maintaining certain savings rate and investment structure, which would ensure their economic transition to mature economies within a short span of two or three decades.

Contemporary experience shows that such prescriptions did not have much merit as countries like India which attained the requisite saving-investment structure could not reach the next stage even after 40 years.

Moreover, Rostow was not offering any explanation of systematic transition through the course of history. Unlike in Marx, there was no unified structure of method trying to explain different "stages" of socio-economic transition (from one mode of production to the other). Rostow does not go into the analysis of what causes the transformation of one stage to another in any systematic manner. In fact these stages hardly have any analytical value—at best they are descriptive categories. Rostow is primarily interested in only one particular transition—the transition to capitalism, which is captured by his take-off stage. The stage immediately preceding or following take-off are hardly independent stages from an analytical point of view in Rostow's framework. The pre-condition stage by its very construct is in terms of explaining take-off later and "take-off" by its very construct needs a stage for maturity for a successful take-off.

Check Your Progress 4

1) What are the main stages of growth in Rostow's scheme?

.....
.....
.....
.....

2) What are the main characteristics of the take-off stage?

.....
.....
.....
.....
.....
.....

3) What are the main criticisms of Rostow's stages of growth?

.....
.....
.....
.....

14.6 GERSCHENKRON'S THEORY OF STAGES OF DEVELOPMENT

Alexander Gerschenkron's analysis of the development of societies stemmed from the understanding that countries embarked upon industrialisation starting from different levels of economic backwardness. These differences were of crucial significance for the nature of subsequent development. The course and character of industrialisation varied depending on the degree of backwardness from which a country started its industrial development. These variations were summarized in the form of certain propositions.

14.6.1 Gerschenkron's Propositions

1) The more backward a country's economy, the more likely is its industrialisation to start discontinuously. It will start as a great sudden spurt with manufacturing output proceeding at a relatively high rate of growth.

2) The more backward a country's economy, the more pronounced is the stress in its industrialisation on bigness of both plant and enterprise.

- 3) The more backward a country's economy, the greater is the stress upon producers goods as against consumers goods.
- 4) The more backward a country's economy, the heavier is the pressure on the levels of consumption of the populations.
- 5) The more backward a country's economy, the greater is the part played by special institutional factors designed to increase supply of capital to the nascent industries. In addition, to provide them with less decentralised and better informed entrepreneurial guidance; the more backward the country, the more pronounced is the coerciveness and comprehensiveness of those factors.
- 6) The more backward a country, the less likely is its agriculture to play any active role by offering to the growing industries the advantages of an expanding industrial market based in turn on the rising productivity of agricultural labour.

14.6.2 The Role of Institutions

While it is usually assumed that there are a number of prerequisites or preconditions for economic growth, Gerschenkron's approach says that **relative backwardness** of a country works as an impetus for the creation of substitutes for these lacking preconditions. The state or banks could compensate for inadequate supplies of capital, skilled labour and entrepreneurship. The role played by various kinds of institutions in compensating for these preconditions would vary with the degree of backwardness of the country. To the extent that the differences in the level of economic advance in the European countries that Gerschenkron studied were sufficiently large, he could arrange these countries along a scale of increasing degrees of backwardness into advanced, moderately backward and very backward.

For example, countries where the Industrial Revolution took place were characterised by the setting up of factories whereas in more backward countries institutional innovations led to the establishment of banks to provide access to capital for industrialisation before factories were set up. In still more backward countries, state intervention played a primary role in providing the institutional structure facilitating a major industrialisation effort. Countries thus went through different "stages" of development from backwardness, depending upon the degree of backwardness itself.

14.6.3 The "Stages" in Gerschenkron's Approach

There are fundamental differences between the "stages" in Gerschenkron's theory and some other theories of stages, notably Rostow's which Gerschenkron himself was at pains to emphasize. As we can see, Gerschenkron's was an attempt, on the basis of historical evidence, to look at how the countries of Europe progressed towards industrialisation and not an attempt at looking at the entire history of economic progress.

It was found that the degree of backwardness determined the stages that a country would go through, the number of these stages being larger the more backward a country was. The speed with which changes inducing movement across these stages took place also increased with the degree of backwardness. These stages were therefore, not repeated from country to country but were determined by the specific historical context of countries. However, from the propositions outlined above, we can see that some of the variations mentioned in the propositions are discrete rather than continuous (denoting the degree of importance of agriculture, vis-a-vis industry, the quantum of production of producers' goods vis-a-vis consumers' goods, all determined by the degree of backwardness) and to this extent the stages can be identified clearly. For example, in proposition 5 above, quantitative differences are clearly associated with qualitative changes. Gerschenkron's division of countries into advanced, moderately backward and very backward are, though based on specific historical observations, generalisable into particular patterns as will be clear from the following diagram:

Diagram 1: Stages and the Degree of Backwardness of Countries

Stages	Advanced Area	Area of moderate backwardness	Area of extreme backwardness
I	Factory	Banks	State
II		Factory	Banks
III			Factory

A diagonal look across the diagram would show that the institution of the factory exists everywhere, irrespective of the degree of initial backwardness. Theories that are only interested in looking at industrialisation as the setting up of a strong manufacturing enterprise would only concentrate on the stage of the setting up of the factory system, which would represent the same stage for all countries. As we can see, the stages in Gerschenkron are not those that every country would pass through, as in Rostow's theory of "stages" of economic growth. Given a particular country's degree of backwardness, it would require to go through some of the stages depicted in the diagram, which are determined by particular institutional changes.

The importance of this kind of approach lies in the emphasis placed on what goes on behind industrialisation and the analysis of institutional changes that facilitate industrialisation.

Check Your Progress 5

- 1) Mention any three of the propositions on which Gerschenkron bases his theory of "stages of development"?

.....

.....

.....

.....

.....

.....

- 2) Explain what Gerschenkron means by the proposition that relative backwardness of a country works as an impetus for the creation of a substitute structure for the preconditions to industrialisation.

.....

.....

.....

.....

- 3) What are the fundamental differences between the approach to "stages of development" in Rostow and Gerschenkron?

.....

.....

.....

.....

.....

14.7 LET US SUM US

We have seen that there is little unanimity in defining, characterising, or even

hardly any consensus, is it all meaningful to devote attention to "theories" of stages of development?

There is not much point, perhaps, in trying to frame development strategies or policies based on the characteristics of these stages (as attempted by Rostow, for example).

Further, neither should this entire area be treated as a body of alternative and contesting theories of progress. Yet, in as much as they are attempts to analyze long-term dynamics, be it in specific or in general terms, they are in some sense, comparable.

Without making an explicit value judgement, one can say that if the enquiry into stages of development has to serve a meaningful purpose, it should be more concerned with identifying the essence of the dynamic processes within a stage and that in the transition between stages, rather than just classifying these stages as mere historical categories.

14.8 KEY WORDS

Serf: a worker on land, who though not wholly owned, unlike a slave, nevertheless has political and legal constraints in leaving the land.

Surplus Product: product over and above what is necessary for replacement and maintenance of the objects of labour. Sometimes it is taken to mean product over and above what is paid as wages.

14.9 SOME USEFUL BOOKS

Bottomore, T.B. (1972): *Sociology: A Guide to Problems and Literature*, Ch. 7, George Allen and Unwin Ltd., London.

Cohen, G.A., (1978): *Karl Marx's Theory of History*, OUP, Oxford.

Gerschenkron, Alexander (1962): *Economic Backwardness in Historical Perspective*, Cambridge, Mass., Massachusetts, Harvard University Press.

Hindess, B. and Hirst, P.Q. (1975): *Pre Capitalist Modes of Production*, Routledge and Kegan Paul.

Hoselitz, F., (1969): *Theories of Stages of Economic Growth* in Hoselitz, Spangler, et.al (eds.)

Marx, K. (1971): 'Preface' to *A Contribution to the Critique of Political Economy*, London, Lawrence and Wishart.

Rostow, W.W. (1971): *The Stages of Economic Growth: A Non-Communist manifesto*, second edition, Cambridge University Press.

14.10 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) Objects of labour are resources existing in nature like land minerals, metals. Means of labour are instruments, equipments or implements which men use to act upon objects of labour.
- 2) Means of labour and objects of labour together make up the material basis of production, called the means of production. Means of production coupled with labour power goes to make the forces of production. Roughly forces of production denote technology plus the skills, idea and productive capacity.

- 3) A specific mode of production is given by the existing forces of production and production relations. The forces of production and production relations together determine the mode of production. Once the relation between the forces of production and production relations undergo a change, the structure of the mode of production changes as well.

Check Your Progress 2

- 1) **Hint:** read section 13.3.2 in the text and answer.
- 2) Extra-economic coercion had to be applied because the serfs actually occupied the land they worked on and could determine how to work the land social custom and stage power were two forms of this extra-economic coercion.
- 3) **Hint:** read section 13.3.4 in the text and answer

Check Your Progress 3

- 1) Broadly the origin and development of the German historical school took place with the rise of nationalism in Germany and as a reaction against English classical economics. They criticised the deductive methods of the English classical school and held that since the historical experience of each country is unique, there cannot be any universal laws.
- 2) List's five stages were: 1) the savage stage, 2) the pastoral stage, 3) the agricultural stage, 4) the agricultural and manufacturing stage and 5) the agricultural, manufacturing and commercial stage. Hildebrand's stages were: 1) natural or faster economy, 2) money economy, and 3) credit economy Bucher's stages were 1) the stage of the independent domestic or household economy 2) the stage of town economy and 3) the stage of natural economy.
- 3) **Hint:** read section 13.4.4 in the text and answer.

Check Your Progress 4

- 1) The main stages of growth in Rostow's scheme are: 1) traditional society 2) pre-conditions for take-off 3) take-off 4) the drive to maturity and 5) the age of high mass consumption
- 2) The main characteristics of the take-off stage are:
 - growth becomes normal condition and forces of production expand
 - industries expand rapidly yielding reinventible project
 - savings rise to about 10 percent of national income and
 - new techniques spread in 60th agricultural and industry
- 3) **Hint:** read section 13.5.6 in the text and answer

Check Your Progress 5

- 1) **Hint:** read section 13.6.1 in the text and answer
- 2) **Hint:** read section 13.6.2 in the text and answer
- 3) The fundamental differences in Rostow's and Gerschenkron's approaches to the stages of development are: firstly, Gerschenkron focused on the experience of Europe and not on the entire history of economic progress, and that his scheme is not directly linear unlike that of Rostow's. The relative backwardness of a country determines the course and character of its industrialisation.

UNIT 15 COLONIAL TRADE AND TRANSFER FROM THE 16TH TO THE 18TH CENTURY

Structure

- 15.0 Objectives
- 15.1 Introduction
- 15.2 The Colonial System
 - 15.2.1 The Historical and Continuing Necessity of Trade for European Nations
 - 15.2.2 The Price-Inflation in the 16th Century
 - 15.2.3 The Civil War and the Navigation Acts
- 15.3 Mercantilist Thought, Triangular Trade and Transfer
 - 15.3.1 The Economic Ideas of the Mercantilists
 - 15.3.2 Triangular Trade in the 18th Century
 - 15.3.3 The Contribution of Colonial Transfers to Capital Formation
- 15.4 Let Us Sum Up
- 15.5 Key Words
- 15.6 Some Useful Books
- 15.7 Answers/Hints to Check Your Progress Exercises

15.0 OBJECTIVES

This unit will give you an idea of :

- The historical origins of the system of colonial domination exercised by Britain before the Industrial Revolution
- The economic theory corresponding to these conditions, known as Mercantilism
- The part played by transfers from the colonies in financing Industrial Revolution and later, capital exports from Britain.

15.1 INTRODUCTION

The industrialisation of Britain, which pioneered the Industrial Revolution, was preceded and accompanied by a rapid development of trade with other nations and territories; an increasing part of this trade in the course of the period being considered, was with colonised countries. The question of the relationship of this fast-growing network of trade relations, to British industrialisation, has been of great interest to economic historians and to development theorists alike. There is a general consensus that the plunder and loot of today's developing countries since the 16th century contributed substantially to the early accumulation of capital in Britain and in the other W. European countries; but there is more controversy regarding the continuing contribution of unequal exchange and of transfers from the colonies to industrial revolution from the end of the 18th century. We will confine ourselves below to a discussion of the Mercantilist period of early capital accumulation from the 16th to the 18th centuries and also take up the question of the extent of transfer from the colonies during the Industrial Revolution.

15.2 THE COLONIAL SYSTEM

In this section we will draw upon the work of not only British economic historians but also that of scholars from other, including colonised countries on the colonial system.

15.2.1 The Historical and Continuing Necessity of Trade for European Nations

The search for new trade routes to Asia during the 15th century in Europe arose in essence from the high degree of dependence for the preservation of basic food, on spices which could not be grown in the cold European climate. As we have seen earlier in Unit 1, the productivity of late medieval agriculture in Europe was extremely low owing to a combination of factors:

- a) one-third to one-half of land had to be left fallow to recover fertility because there was a shortage of organic manures, which arose from
- b) the inability to produce enough fodder to maintain livestock through the winter months, hence slaughtering of a part of the livestock was necessary and the meat had to be preserved by the copious use of salt and spices. Further,
- c) the problem of low yields was compounded by the high seed-yield ratio, such that a quarter and even up to one-third of the grain harvest had to be set aside for the next season's seed (compared to only one-tenth in tropical areas) which in turn meant that the competition between foodgrains for human consumption and feedgrains or fodder crops, remained acute and was resolved in favour of foodgrains, thus completing the vicious circle.

In such a situation of low productivity, and the need to preserve meat, spices were a necessity, not a luxury for Europeans at that time. Lacking any access to tropical bio-diversity, their consumption basket was severely limited. The diet was high in calories but without variety and very monotonous. B.H. Slicher van Bath, an authority on medieval agriculture, gives us data on the diet of both the nobility and of serfs in 16th century Sweden and Germany. The data shows the consumption of large quantities of meat, over 90% of it in dried and salted form, bread and highly salted butter which was often rancid, and a beer consumption per head which was 40 times higher than today, required to wash down the saline food. (*The Agrarian History of Western Europe, A.D. 650-1800*). The absence of fresh vegetables and fruit during the winter months produced vitamin deficiency diseases. In contrast both the nobility and the ordinary people had access to a far more diversified basket of consumption in semi-tropical and tropical countries. In 16th century India, Abu'l Fazl's *Ain-i-Akbari*, part of the *Akbarnama*, gives us in *Ain* 27 and 28 the prices of certain essential commodities, including as many as 26 common varieties of vegetables and 35 of fruits, the list being by no means exhaustive.

The diet and standards of life of the West Europeans have been transformed during the last 400 years. This is partly owing to improvements in their domestic agriculture permitting the maintenance of livestock through winter and hot-house cultivation of semi-tropical and tropical countries. In 16th century India, Abu'l Fazl's *Ain-i-Akbari*, improvement owing to their increasing access through trade, to the bio-diversity of the semi-tropical and tropical areas of the world. This access was historically secured through the monopolisation of trade routes and the conquest of colonies, which we will briefly discuss below in the context of Britain, the earliest and most successful colonising European country. It was consolidated through the large-scale dispersal of commercially valuable tropical plants (rubber, coffee, tea, sugarcane, tobacco, cotton etc.) from their regions of origin to other parts of the colonised world for production on a plantation basis. These products were exported to the benefit of the industrialising European countries. Trade was thus extremely important for the latter

countries in a way that it was not for the larger Asian nations in particular such as India and China, which could grow everything that Europe could and in addition enjoyed tropical bio-diversity. Indeed trade continues to be extremely important for W. Europe and North America which are to this day heavily import dependent on the much poorer developing countries for the consumption goods which are the material expression of their high living standards. If all trade were to cease today, these high living standards would collapse to near-medieval levels. The products of tropical imported origin which every W. European and N. American household uses daily, would then no longer be available: beverages like tea, coffee, cocoa, fruit juices; vegetables and fruit in fresh, processed and frozen form; sea-food; sugar, chocolate and sugar-based alcoholic beverages; spices and flavourings; nuts and cereals; cotton, mixed fabrics and silk; goods using rubber; tropical furniture hardwoods; and many luxuries like decorative plants, cut flowers and ornamental fish. The characteristic of these primary products is that no domestic production and hence import substitution within W. Europe is possible because the cold climate does not permit these to be grown. (Chemical substitutes for some, like aniline dyes for indigo, have been tried but they have long-run toxicity problems.)

When this factual background is borne in mind you will find it easier to understand the single-minded and often ruthless pursuit of control over the tropical areas of the world in particular, and the consistent efforts to obtain valuable tropical commodities on the best terms to themselves, which has been displayed historically by the W. European nations. The countries of E. Europe in contrast persisted longer with feudal economic and social structures, never had colonies or access on easy terms to tropical bio-diversity; this is reflected in their continuing poorer average consumption basket. Of course, the motivations for pursuing colonial policies were not limited to securing access to tropical bio-diversity and forest and mineral resources alone but also included other objectives such as access to captive markets and to the means of trading and investing in the then developing countries of the Continent and N. America.

15.2.2 The Price-Inflation in the 16th Century

The tremendous expansion of trade which took place after the accidental discovery of the Americas by Europeans and the circumnavigation of the earth, was qualitatively different from earlier trade. For, it was characterised by colonisation and the growth of the slave-labour based plantation system for the production of tropical commodities in increasing demand in Europe. The bitter wars which were fought by the W. European nations for control over the lucrative new trade in tropical goods and in the slaves for producing those goods, resulted in the eventual domination of England. She followed a consistent national policy of Mercantilism which led to England's success over her rivals. We will discuss the content of mercantilist policies a little later. Let us first see what the main economic developments in the 16th century were which stimulated capitalist activities both in production and in trade.

A number of trading companies were formed in each W. European country in the course of the 16th century on the basis of royal charter conferring exclusive monopoly of trade with the company concerned, in the relevant region. In England the year 1553 saw the formation of both the Russia Co. and the Africa Co., the former giving the exclusive monopoly of trade in Russian grain and furs while the Africa Co. was to grow into one of the most lucrative enterprises of all time with its trade in human merchandise. In 1577 the Levant Co. was given by charter the monopoly of trade with the countries bordering the Eastern Mediterranean. In 1578, the Eastland Co. was granted a similar monopoly of trade with the Baltic countries. The Spanish Co. was formed in 1592, and the East India Co. in 1600. The last is of special importance for us since India's fortunes for the next three centuries were to be affected by it.

The 16th century is dominated by the price-inflation, which is termed the 16th century 'price-revolution' by economic historians. The basic reason for the secular trend of rise in Europe in the prices of necessities and in the general price level, was the cheapening of the precious metals as a result of a fall in their cost of production

after regular mining of gold and silver was started in S. America. When the Spanish and Portuguese conquistadores overran the civilisation of the Aztec in central America and the Inca in Peru and Bolivia, they initially looted the hoards of precious metals in royal exchequers, and proceeded on a campaign of killing those who offered resistance. The surviving labour force was enslaved and put to work in the gold and silver mines in Potosi and elsewhere. The regular supply of precious metals which started flowing back to Iberia was partly diverted to other parts of Europe by the pirates who intercepted the returning galleons. The then queen of England, Elizabeth I, had shares in Drake and Hawkins' piratical expeditions and it is estimated that these yielded as much as a sixth of the total earnings England had from her exports at that time.

The cheapening of the precious metals owing to a fall in their cost of production was the same as the rise in the ratios in which metallic money exchanged for goods, that is it meant a rise in prices. Between 1500 and 1600 the price of grain trebled in Europe and doubled again in the next 50 years. This may seem a low rate of inflation compared to modern rates; but compared to the great stability in trends in economic variables in the medieval period, it was indeed a revolution. Keynes refers to it as one of the earliest examples of a 'profit inflation', by which is meant a situation where final output prices rise faster than the wages of labourers producing those products, thus increasing the share of profits out of the value of net output. J.M. Keynes discussed the concept of profit inflation in his book, *Treatise on Money*. This stimulated the growth of capitalist production. Real wages of the workers in the nascent manufactories were halved during the 16th century, because at this early date no trade unions of workers existed. In fact legislation put maximum limits to money wages while there were no minimum limits. This increased the distress of the labouring poor for with inflation the earlier maximum limits on money wages became quite unrealistic if a worker was to get enough to eat. The supply of hired labour itself was increasing in this period because the 16th century 'enclosures' in England got under way with the relatively faster rise for a time in the price of wool compared to other products, leading to the eviction of small tenants and conversion of grain-land to sheep pastures.

15.2.3 The Civil War and the Navigation Acts

England underwent a Civil War from 1640 to 1660, whose importance is underestimated in conventional historical sources. In effect, the Civil War in England brought about a far reaching destruction of feudal political power; it initiated a new era of aggressively nationalist economic policies of pursuing wars for control over trade routes and overseas territories. In view of the fact that this took place more than a century before the justly famed Revolution of 1789 in France, it is perhaps understandable why England got a head-start over France in the race for colonies. The only serious rival England had in the 17th century was the Dutch Republic, which before 1650 was forging ahead both as a woollen textile manufacturing and financial centre and in the lucrative control over trade routes to the Baltic, the Americas and the East Indies.

The Civil War in England was fought essentially by the rising classes of merchant-manufacturers, small capitalists and profit-minded landed squires, against feudal absolutism. Initially the aim was only a reformed monarchy, but the monarch insisted on the 'divine right of Kings', refused to be accountable to Parliament and sought military support from abroad. This led to the civil war, with the King and aristocracy, known as the Royalist side, fighting a hastily formed but highly motivated 'New Model Army' under the leadership of Cromwell for the Parliamentary side. Victory lay with the progressive side, and the King was tried and executed along with his leading Ministers. For a period of 11 years, from 1649 to 1660, England was a republic of sorts, and the term 'Commonwealth' was coined to describe the state. Even though the monarchy was nominally restored after 1660, it no longer had even a fraction of the powers it had exercised earlier. Parliament, dominated by the increasingly capitalist-minded gentry, decided economic and other policy.

During the Commonwealth under Cromwell, an aggressively nationalist policy of overseas expansionism and centralised control over colonies, was formulated and put

into effect. The **Navigation Act of 1651**, amended in 1655, was a much more comprehensive economic policy measure than its name indicates. It laid down that all colonies were to be subordinated to Parliament and all trade to and from the colonies was to be monopolised by English shipping. It also gave the colonies the monopoly of access to England for particular goods. It represented for the first time the expression of a coherent **national imperial policy** as opposed to the scattered and separate interests of the various monopoly trading companies (see Christopher Hill, *Reformation to Industrial Revolution*). The Navigation Acts were to remain the cornerstone of the colonial system for more than a century. As regards expansion, Ireland was conquered and its land passed to English landlords whose tenants the Irish farmers became. Millions of pounds of rent extracted from the Irish tenants flowed to England in the form of an export surplus of corn and dairy products. Under an Act of 1696, Ireland was forbidden to export cattle and dairy products to any other country than England, and she was forbidden to manufacture woollen textiles for herself, being obliged to rely on imports from England. The traditional industry all but ceased to exist; linen however was not subject to the ban and linen manufacturing developed with English capital. These restrictions on Irish trade were strictly enforced through naval blockade.

The wars fought successfully by England against the Dutch between 1672 to 1684, served to breach in England's favour the Dutch monopoly over the lucrative Baltic trade in furs and fish, as well as breaking the Dutch monopoly over the slave trade from the W. African coast and the spice trade from the E. Indies. This was preceded by the capture of Dunkirk (strategically located for shipping passing through the English channel), and the seizure of Jamaica in the W. Indies. Domination over Portugal was secured with victory in the War of the Spanish Succession, and England both gained access to the vast Iberian Empire in S. America and obtained the highly coveted *Asiento*, or monopoly right of supplying slaves from W. Africa to the S. American colonies of Spain and Portugal. A marriage of convenience between Charles the Second of England and Catherine of Braganza of Portugal brought Bombay, a Portuguese Colony, as part of the dowry. As Christopher Hill puts it, 'the nucleus of all the future colonies was in place by 1696'.

The colonies including the N. American colonies, were subjected to the same set of regulations as Ireland, regulations which forbade the manufacture of all goods competing with English products and which ensured England's monopoly access to colonial markets for these goods. This meant that even if a commodity could be produced much more cheaply in the colony because both local raw materials and labour were available, the colony was instead obliged to import it from England, many thousands of miles away. Moreover, they had to pay for the shipping and insurance charges which were, under the Navigation Acts, a monopoly of England alone. N. America was forbidden to manufacture woollen textiles, iron, even hats and pins. The Caribbean slave population despite the warm climate was obliged to wear English wool until the reexport of Asian textiles to them from England provided some respite. Although the slave plantations of the Caribbean colonies produced sugarcane, the refining of the molasses to produce sugar was done in England, as was the case with rum distilling, in the initial decades. (Eric Williams, *Capitalism and Slavery*). It will be clear from the examples given that the basic objective of these policies was to encourage manufacturing production within England, regardless of whether it was at a relatively higher cost (and hence less efficient) than elsewhere, in order to generate domestic output and employment. The domestic landlords were also protected against cheaper agricultural products from the Continent.

Check Your Progress 1

- 1) What were the economic reasons that prompted England to colonise the tropical countries?

.....
.....
.....
.....

- 2) What were the main economic developments in the sixteenth century which stimulated capitalist activities in production and trade ?

- 3) What were the economic implication of the Seventeenth Century Civil War that England went through ?

15.3 MERCANTILIST THOUGHT, TRIANGULAR TRADE AND TRANSFER

In this section, we will see how the mercantilists—the leading group of 17th-18th century British economists—played a major role in policy making towards the colonies. Then, we shall present an overview of the triangular pattern of trade that characterised Britain's trade with her colonies. Finally, you will read about the extent to which the extraction from colonies by Britain provided capital to finance the first industrial revolution.

15.3.1 The Economic Ideas of the Mercantilists

You will already have gained some idea of the content of Mercantilist policies from the above description. The mercantilists initially tended to think of the act of trading itself as a source of wealth; whereas in fact, the wealth concerned was produced by the pre-capitalist communities with which England traded in Asia, to whom payment was made below the value of their product, or was created by the labour of slaves maintained at bare subsistence level during the short span of their lives. Much of the very high profits, apparently obtained by the act of trading, in fact arose from two factors: the widespread use of coercion to force producers abroad to part with their goods at prices below their cost of production, and the exercise of monopoly backed by armed state power. This may be defined as the essence of 'unequal exchange'.

The slave trade was in a special category by itself because, considered as a

commodity like any other (as from the Europeans' viewpoint at that time), this human 'commodity' was actually obtained at zero 'production cost' and only the cost of transport had to be paid. This is because the cost of raising these persons to adulthood was borne by their rural communities in West Africa, from which they were forcibly kidnapped by the Arab slave traders who supplied the European slavers against payment in weapons, cloth and spirits. This payment need have been only sufficient to compensate for the cost of the raiding expeditions. Packed into the holds of English ships where many died, they were transported to the W. Indies, Brazil and the Southern states of the N. American colonies. There a slave could be sold for, on average, five times what the slaver had paid at the W. African ports, that is, at a profit rate of 400% on the initial outlay, and the over 350% if the shipping cost per slave is included (see Eric Williams *Capitalism and Slavery*) Now these very high profit rates reflected precisely the fact that the economic worth to the purchaser of the slave-commodity, embodying so many years of labouring capacity, far exceeded the mere transport costs which had been paid by the trader; he had paid nothing to the W. African communities and had obtained their manpower and womanpower free through the exercise of force. We have defined unequal exchange as payment below the cost of production to the subordinated agent; the slave trade represented the extreme limiting case of zero payment towards the cost of production, and involved only the cost of transport. From the economic point of view this explains the high degree of lucrativeness of the slave trade, which in the words of Adam Smith, 'raised the Mercantilist system to its full pinnacle of glory' (*The Wealth of Nations*).

The early Mercantilist writers, known as the Bullionists, thought of the inflow of gold into their country as being a desirable end in itself. Later the emphasis shifted more towards the desirability of having an export surplus and increasing this export surplus as much as possible, while the consequent inflow of bullion (from other countries paying for their import surplus with Britain) became secondary. The regulations forbidding colonial manufactures were designed to increase England's exports to the colonies which as we have seen, had to use English goods even if potential domestic production capacity existed.

The Mercantilists also laid stress on the need to raise exportables' prices compared to importables' prices as much as possible, that is, they advocated turning the terms of trade against the countries from which they imported and in their own favour. This objective of raising relative prices of exportables might seem to be in contradiction with the other declared objective of increasing the export surplus. For, under conditions of normal trade, the importing countries could be expected to reduce their purchases of English exportables as their prices rose. Then English export earnings would fall. In modern times the suggested policy for raising exports from a country relative to imports, i.e. of increasing the export surplus is to lower the price of exportables relative to that of importables through devaluation of the currency (and even so trade balance will improve only if demand abroad for the country's exports is price elastic and demand within the country for imports is similarly price-elastic). How can we explain, then, the fact that the Mercantilists advocated a precisely opposite policy of raising, not lowering, relative price of exportables and still saw no conflict with, at the same time, improving the trade balance?

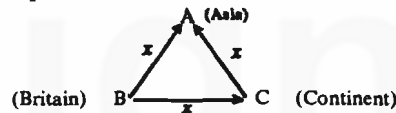
The answer lies in the fact that the Mercantilists took it for granted that much of the trade they were talking about was colonial trade where the countries concerned had no choice about whether they wished to import English goods or not, but had to import regardless of the price. Foreign (i.e. non-English) demand in short was assumed to be inelastic, in the extreme case to have zero price elasticity, and was expected to be kept that way through the use of force. This brings us to the last important feature of Mercantilist thought, namely the idea that there should be a large degree of State intervention in and regulation of the economy in the interests of maintaining national economic hegemony and high rates of profit. This was the opposite of Adam Smith's idea of the invisible hand of the market which would take care of the allocation of resources. The idea of a marginal role for the state, was totally antithetical to Mercantilist thought. In fact such ideas could not arise until economic growth on the basis of Mercantilism had itself gone far enough such that the myriad small capitalists thrown up by that growth, began to feel constrained by the existing monopolies and restrictions on trade, to demand a change in the policy regime.

Many of the Mercantilist writers were closely associated themselves with the monopoly trading companies.

15.3.2 Triangular Trade in the 18th Century

The trade network encompassing Britain and the world which developed during the 18th century prior to the Industrial Revolution, was characterised by the absence of bilateral balancing. Instead there were a number of trilateral trade patterns. By 'bilateral balancing' is meant the typical situation depicted in textbook two-country models of trade, in which country A, trading with country B, must necessarily balance its balance of payments with it. For example if country A has a trade deficit or more generally a current account deficit vis-a-vis country B, it must necessarily either have a matching bullion outflow to B to pay for this, or it must borrow from B, or have a combination of the two. In reality however Britain, call it country B, operated a more complex set of trade flows in which she had surpluses vis-vis some regions A which were used to pay for her deficits vis-a-vis other regions C, given that region A had surplus vis-a-vis C. In these trilateral trade patterns, the control over colonial economic surpluses was of crucial importance.

To clarify the above let us consider Asia as region A, denote Britain as country B, and the European Continent as region C. Then, the triangular pattern of trade balancing would look as follows, with the arrow pointing to the country with the trade surplus in each pair:



In the diagram above, Asia has a trade surplus of x million pounds with the Continent, while the Continent has a trade surplus of x million pounds with Britain. The latter country can pay off the Continent provided it has a trade surplus of the same amount with Asia, thus completing the trade and payments triangle. The basic problem for England during the 17th and upto the middle of the 18th century was that the direction of the arrow denoting its trade relation with Asia was in fact the other way around, namely England had a trade deficit with Asia, not a trade surplus. Neither China nor India could be induced to absorb English goods in sufficient quantity to offset the increasing demand in England for tea, cotton and silk textiles, porcelain, saltpetre and other goods. (Not all of this was consumed directly in England; a large part was reexported against essential imports from the Continent, as we will see below). The East India Co. tried to minimise the value of the trade deficit by underpaying the artisans from whom they bought these goods, exercising force in securing goods, and refusing to pay local customs duties. Nevertheless the deficit remained and had to be settled by bullion outflow from England to Asia.

This situation was changed drastically when the right of collecting the land revenue and other revenues was acquired by the East India Co. in 1765 after the defeat of the Nawab of Bengal in the 1757 Battle of Plassey. From being a mere trading company, the East India Co. now obtained the rights of sovereignty. It continued to trade in the same goods as before, but the economic content of its activities had changed drastically. On average, during the last quarter of the 18th century, one-third of the net revenues of Bengal, was used to purchase the goods in which the Company traded. (Net revenue was the gross revenue collections minus the costs of salaries and commissions to the revenue collecting agents and the *nazrana* to the Mughal emperor). This meant that the East India Co. no longer had to advance any funds out of its own trading profits to purchase exportables (as in any normal trading) but got these goods free, since the very same people from whom it bought these goods, paid the taxes to the Company out of which the goods were purchased.

There were two other important trade triangles in the 18th century: the W. Indies—Britain—N. America trade triangle, and the Britain—W. Africa—W. Indies & S. America trade triangle. In the first of these, the W. Indies were obliged to specialise in the slave-based plantation production of valuable tropical crops in growing demand in developing Europe, such as sugarcane, cotton, tobacco, mahogany etc. These islands were thus deficit in food production; foodgrains were imported from the N. American colonies, which in turn were obliged to import their manufactured goods from England. In the second trade triangle, slaves were kidnapped at no cost

and sold to the European traders against payment, as earlier described, from the W. African hinterland against payment in English spirits, weapons and cloth. When they were transported and sold in the W. Indies and in Brazil where the surplus product of their labour went as an export surplus to England, while the required manufactures in the Caribbean and S. America (cloth, chains, handcuffs and fetters) were imported mandatorily from England.

15.3.3 The Contribution of Colonial Transfers to Capital Formation

Most economic historians of Britain would readily concede that there was an early phase of 'plunder and loot' of the colonies, especially of India. Since the English Parliament itself under Burke's leadership, impeached Warren Hastings for the wrongful oppression of and plundering the treasuries of local rulers, and for oppressing the peasants, there is little scope for denial of this phase of 'plunder and loot'. Clive amassed a huge personal fortune by similar means and on returning to England, purchased landed estates and a seat in Parliament. These wealthy employees of the East India Co. came to be called 'The Nabobs'.

These incidents of 'plunder and loot' were however episodic and once-for-all affairs. Of far greater importance was the systematic transfer year after year, of a part of the taxation revenues of India to Britain in the form of an unrequited export surplus of goods. In the case of the plantation system of the W. Indies, however the main mechanism was not collection of revenue from peasants but the appropriation of slave-rent. The entire gross output value less production costs including the bare-subsistence maintenance of slaves constituted the slave-rent. The slavers remitted this slave-rent to Britain similarly through an export surplus of goods. The economic historians of Britain have totally neglected the transfer from India and from the W. Indies, and its contribution to British industrialisation. The magnitude of the annual transfer was in fact very large compared to the British Gross Domestic Product and Gross Domestic Capital Formation at that time. The neglect of the role of the transfer arises from a conceptual failure on the part of the historians to recognise the transfer as transfer and to treat it erroneously instead as 'normal trade'. A typical example of a cursory and theoretically incorrect treatment of the question may be found in a standard textbook read by British students (Ch. 5 on 'Overseas Trade and empire', in R. Floud and D. McCloskey eds., *The Economic History of Britain since 1700*).

If indeed the import surplus into Britain from the tropical colonies had been normal trade, this import surplus would have had to be paid for by Britain either through a matching-outflow of bullion, or a positive balance on account of invisibles earnings, or borrowing from the colonies—or a combination of these. Otherwise, the balance of payments would not have balanced. In fact however none of these happened, because it was transfer and not normal trade that the import surplus represented. In the modern world if any country, such as Britain today, was to pile up an increasing trade deficit amounting to 3% to 4% of its GDP, against any set of countries, this would be a cause for great concern and strenuous efforts would be undertaken to reduce the deficit. The increasing import surplus of this magnitude from the colonies, on the contrary, was taken (rightly) as an indicator of increasing prosperity in Britain, and economists at that time were not at all worried about the question of financing this deficit.

They were quite right not to be worried because as we have seen, after 1765, when the taxation collection rights in Bengal were acquired by Clive from the Mughal Emperor, England no longer needed bullion outflow to pay for her import surplus from this region because she used a part of the colonial tax revenue to purchase directly the goods she traded in from Bengal. This meant that a part of the tax revenue was being transferred to Britain in the form of an export surplus of goods from India. In effect Britain did not have to pay for this import surplus: the Indian tax-payers financed it. All Britain incurred by way of cost was the transport charges. These goods were sold, of course, at their full value to the final purchasers. It is incorrect to argue that only the East India Co., or only the Africa Co., benefited. What Britain gained thereby has two sides to it. First, from the point of view of the national economy, she obtained a virtually costless supply of valuable tropical wage-

goods and raw materials most of which she could not ever have produced domestically owing to her climate: among wage-goods, sugar, tea, foodgrains and tobacco were the most important; cheap rum became an essential consumption item for sailors. Among raw materials, cotton, indigo, jute and timbers were prominent. The leading sector of the Industrial Revolution, cotton textiles, could scarcely have got off the ground without a plentiful supply of the entirely imported raw material, which could not be grown in Britain. Secondly, Britain's own domestically produced exportables were in inelastic demand on the European Continent which was her most important equal trading partner, whereas British demand for strategic materials from the Continent like bar iron, naval supplies like hemp for ropes, pitch and tar, timber for shipbuilding, and other goods, was increasing and tended to move her trade balance in increasing deficit. Here the reexport of tropical goods embodying the transfer, came to the rescue since these goods were in elastic demand on the Continent (see Phyllis Deane 1969). The high proportion of reexports to total imports, will be clear from the following table :

Table 15.1 : Annual average Imports and reexports, 1765-99,
Pounds(Official values in Constant 1700

Period	Imports M	Re-exports R	Percentage R/M
1765-69	11.671	4.580	39.2
1770-74	12.600	5.627	44.7
1775-79	12.464	5.086	40.8
1780-84	12.635	4.110	32.5
1785-89	17.143	4.949	28.9
1790-94	20.001	6.842	34.2
1795-99	20.326	12.008	59.1
1800-04	30.400	15.930	52.4
Total	137.240	59.132	43.1

Source: Mitchell and Deane 1962 'Abstract of British Historical Statistics, pp. 280-281. Calculated from annual series.

From Table 15.1 it can be seen that re-exports (which were almost entirely of tropical goods) made up on average two-fifths of total imports; it would be a much higher proportion of tropical imports. According to the data in Deane 1969, at least 85% of all reexports went to the Continent throughout the 18th century for purchasing strategic raw materials and for importing foodgrains.

An interesting estimate has been made by Sayera Habib of the proportion of transfer from Asia and W Indies, to capital formation in Britain (*Colonial Exploitation and Capital Formation in England in the Early Stages of the Industrial Revolution*). She finds that in the year 1801, it amounted to as high as 5% of British GDP and 71% of domestic capital formation. Taking the annual time-series data on British trade from Mitchell and Deane's *Abstract of British Historical Statistics*, the following five-yearly averages are obtained of the annual import surplus into Britain from Asia and the W. Indies:

Table 15.2: Import surplus into Britain from Asia and the W. Indies
(Five-year average, constant 1700 prices, million pounds)

Period	Asia (M - X)	W.Indies (M -X)	Combined M - X)
1780-84	0.762	1.211	1.973
1785-89	1.552	2.348	3.900
1790-94	0.948	1.411	2.359
1795-99	2.872	0.797	3.688
1800-04	2.898	3.821	6.719
1805-09	2.777	2.889	5.666

Source: Mitchell and Deane (1962) p. 311

You will observe that there is a large jump in the import surplus from India after the Permanent Settlement of Bengal in 1793. The estimates of British Gross Domestic Product (GDP) are available only from 1801, in current prices. To estimate the transfer as measured by the combined import surplus from the W. Indies and

Asia and to express it as a percentage of the GDP, the transfer first has to be expressed in 1801 prices. The per capita GDP in 1801 was 25 pounds and the total GDP was 232 million pounds. The value of the combined transfer for the period 1795-1804 works out to an annual average of 5.77 m. pounds, which S. Habib adjusts for price rise (upto 1797) and for smuggling, obtaining a current value of 11.54 m. pounds. This works out to 4.97% of the GDP of 1801. Deane estimated that domestic capital formation was at most 7% of GDP. Hence the value of the combined transfer works out to 71% of domestic capital formation at that date.

Thus the magnitude of the transfer was very substantial when compared to British income and capital formation. This should not surprise us for Britain was then demographically speaking, a very small country (the population in 1801 was only 9 million). We have seen that Britain had acquired many decades earlier control over the

- highly lucrative slave trade,
- the surpluses generated from the immensely profitable plantation production in the Carribean of tropical products in elastic demand in the European world,
- the revenue collecting rights of an agriculturally prosperous region in India (Bengal and the Northern circars) which was at least five times more populous than England.

Even if we assume that the per capita income in this colonised region of India was only one-tenth of that in Britain, this implies that Britain had acquired the tax-collection rights of an economy whose rural sector alone was half as large as the entire British economy in income-generating capacity.

As Sayera Habib puts it, 'What the British economy gained from colonial wealth was....not landed estates nor even luxuries for aristocratic consumption, but an immense supply of raw materials and wage-goods — a supply inconceivable if Britain did not have colonial tribute to finance it.' In effect, the actual rate of capital formation in Britain was nearly double the recorded rate once the inflow of transfer is taken into account. This is bound to make you wonder whether the 'Industrial Revolution' in Britain would have been such a revolution at all, without the colonial transfer. It might rather have been a process of industrial evolution rather than revolution.

Check Your Progress 2

- 1) What was the 'cost of production' of African slaves as far as the Europeans were concerned? Why?

.....
.....
.....
.....

- 2) How did the British conquest of India enable Britain to finance its investment inspite of maintaining a balance of trade deficit vis-a-vis India?

.....
.....
.....
.....
.....

- 3) Analyse the contribution of tropical countries in the making of the first Industrial Revolution.

.....
.....

.....
.....
.....
.....
4) What are the main tenets of mercantilism ? In what ways is it different from the
laissez faire doctrine of Adam Smith?

.....
.....
.....
.....
.....
.....
.....
.....

5) What is 'unequal exchange' ? Briefly write a note on the colonial pattern of
trade.

.....
.....
.....
.....
.....
.....
.....
.....

6) What is triangular trade ? How is it different from bilateral trade ?

.....
.....
.....
.....

15.4 LET US SUM UP

By reading this Unit you have gained some idea of the importance of access to tropical bio-diversity for the Europeans, owing to the climatic limitations of their own lands which could grow only a restricted range of products. To this day, high living standards in the industrially advanced countries is heavily dependent on their access to our bio-diversity and that of other poor tropical countries. This access was secured by the European nations led by England (which was the first country to undergo a political revolution towards capitalism — the 1640-1660 civil war) through the use of armed force. Tropical areas were colonised, and England was the most successful coloniser of the European nations owing to her ability to mobilise very early, the entire weight of state power to this end.

The extent of transfer from the tropical colonies was very substantial compared to Britain's national income and capital formation during the period of Industrial Revolution. According to a careful estimate, it was as high as 71% of the domestic capital formation in 1801. Since domestic capital formation was 7% of the gross domestic product, the transfer was 4.97% of the British GDP at this date.

15.5 KEY WORDS

Mercantilism: An economic doctrine emphasising active state intervention, maintenance of an export surplus to promote inflow of bullion through economic and extra-economic measures and believing that military strength and bullion are the source of economic and political power.

Nazrana: Urdu for gift

Unequal exchange: Payment below the cost of production, slavery being the extreme form of unequal exchange where no payment is incurred to meet the cost of production.

15.6 SOME USEFUL BOOKS

Hill, C., 1969. *From Reformation to Industrial Revolution, 1530-1780*, Penguin, Harmonds Worth (Pelican Economic History of Britain Vol. 2).

Williams, E., 1966. *Capitalism and Slavery*. Revised Edition, Capricorn Books, New York.

Habib, S., 1975. *Colonial Exploitation and Capital Formation in the Early Stages of the Industrial Revolution*.

Deane, P., 1969. *The First Industrial Revolution*, Cambridge University Press, London.

15.7 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) Read Sub-Section 15.2.1 and answer.
- 2) Read Sub-Section 15.2.2 and answer.
- 3) Read Sub-Section 15.2.3 and answer.

Check Your Progress 2

- 1) Read Sub-Section 15.3.1 and answer.
- 2) Read Sub-Section 15.3.2 and answer.
- 3) Read Section 15.3 and answer.
- 4) Read Sub-Sections 15.3.1 and 15.3.2 and answer.
- 5) Read Sub-Section 15.3.1 and answer.
- 6) Read Sub-Section 15.3.2 and answer.

UNIT 16 THE COLONIAL FINANCING OF CAPITAL EXPORTS IN THE 19TH CENTURY AND SOME THEORIES OF CAPITALISM AND UNDERDEVELOPMENT

Structure

- 16.0 Objectives
- 16.1 Introduction
- 16.2 The Railway Boom and Capital Exports
 - 16.2.1 Importance of the Railway Boom for Britain
 - 16.2.2 The Country Destination of Capital Exports
- 16.3 The Era of Imperialism and Overseas Investment
 - 16.3.1 Imperialism and its Link with Investment
 - 16.3.2 The Colonial Financing of Overseas Investment
- 16.4 Some Theories of Capitalism and Underdevelopment
 - 16.4.1 Linear Development Theories : Rostow and Hicks
 - 16.4.2 Colonies viewed as a Capitalist 'Periphery'
 - 16.4.3 Colonies viewed as Markets
- 16.5 Let Us Sum Up
- 16.6 Key Words
- 16.7 Some Useful Books
- 16.8 Answers/Hints to Check Your Progress Exercises

16.0 OBJECTIVES

After going through this unit, you will be able to :

- discuss the continuing importance of colonies in the era of heavy overseas investment by Britain in the 19th century;
- explain the balancing role played by colonial transfer in the international payments system; and
- analyse the main differences in some theoretical approaches to colonial underdevelopment.

16.1 INTRODUCTION

Sections 16.2 and 16.3 are based on some classic writings on 'Imperialism' like the book of that title by J.A. Hobson, and on the researches of present-day scholars like S.B. Saul, *Studies in British Overseas Trade*. You may wonder why since we have already discussed about imperialism in Unit 3. This is because the question of financing imperialist investment abroad had not been taken up there and will be discussed in this Unit. Section 16.4 is a brief overview of some contrasting theoretical approaches to the question of the relation between today's industrially advanced countries like Britain, and their colonies like India, in particular with respect to the analysis of underdevelopment.

16.2 THE RAILWAY BOOM AND CAPITAL EXPORTS

The Colonial Financing
of Capital Exports in
the 19th Century and some
Theories of Capitalism
and Underdevelopment

The Railway boom started in the 1830's but got seriously under way only in the mid-1840's. During the two decades preceding the railway boom, the British economy was marked by two features. Firstly, although the Industrial Revolution had been barely consolidated by the 1830's, investors in Britain were already facing falling returns within the economy. Secondly, there were acute social and political tensions between the capitalists and the working class. These two features were in fact related, as is explained below.

16.2.1 Importance of the Railway Boom for Britain

By the late 1830's in Britain, the relation between labour and capital was perhaps at its most antagonistic compared to any previous period. As you know from Unit 2, the workers in the factories who were mainly children and women, had to work inhumanly long hours including doing night work, for low wages. Whenever machinery was introduced a number of workers were thrown out of jobs, and it took time for growing production to reabsorb them. The miners lost on average over 1,000 of their workers to fatal accidents every year.

The workers as a whole had initially joined with the manufacturers in the agitation for the reform of Parliament (which was dominated by the landlords) and for the repeal of the Corn Laws which kept bread prices high. They had hoped to get some representation in Parliament, but when the Reform Bill of 1832 was passed they were excluded because this Bill had a stiff clause requiring the possession of property for a man to be eligible to vote. Moreover the New Poor Law of 1834 passed by the manufacturers, made it compulsory for unemployed workers to work in the state work-houses which were like prisons, and they were separated from their families. All this angered the workers and they now agitated separately under the banner of Chartism. This working-class movement (Chartism) was named after the People's Charter drawn up in 1835 by the Workingmen's Association. The Chartists organised labour and there were a series of strikes culminating in an insurrection in 1842, which was militarily suppressed by the Government.

The low wages paid to workers for long hours of work meant high profits for the individual manufacturers, but at the same time created a problem for the economy as a whole, namely the inadequate growth of the home market for manufactures owing to the inadequate growth of the purchasing power of the ordinary workers who made up most of the population. There was after all a limit to the number of suits of clothing the well-to-do minority of people could wear, or the number of houses and carriages they required, or the number of town halls which could be built. The prospects for profitable investment within Britain, of the capitalist's rapidly accumulating surplus funds, were declining at the same time. According to Eric Hobsbawm, by 1840 every year there were '40 million pounds crying out for investment in Britain', more than the entire value of the cotton textile factories and their machinery. Government could borrow money from the public against issue of bonds at only 3.5% rate of interest. It almost seemed as though the fears of the classical economists regarding a falling rate of profit eventually leading to a stationary state, were justified.

It was at this juncture of falling profitability and social unrest, that the Railway boom arrived to life the British economy onto a new trajectory. Hence its great economic and even political importance. The steam engine had been invented by Watt as long ago as 1765, and had been applied since then to the transporting of coal, from the mine pit-heads to canals and ports. But the idea of applying the steam engine to general freight and passenger transport, which we take for granted today, was put into effect only in 1825 with the construction of an experimental line from Darlington to Stockton in England. With the success of the experiment, a veritable boom of railway construction started. There was a small boom during 1825-37 and a large boom from 1845, which by generation employment and fuelling strong growth, took the steam out of the militant workers' movement.

From the viewpoint of absorbing surplus investible funds railway investment was ideal. It was a great guzzler of capital, requiring the laying down of steel rails for the tracks and the manufacture of the locomotives and the rolling stock. And it opened up prospects for increased profitable production not dreamed of by the initial investors, because of its strong and extensive 'backward' as well as 'forward' linkages. By 'backward linkages' we mean the demand for the goods required in railway construction and operation, which grew fast: pig iron, steel, and coal, and the output of the engineering industries. Coal mining was highly labour intensive and the ten-fold growth of coal output in Britain between the 1790's and 1850 for 1 m. tons to 10 m. tons meant a five-fold rise in the number of mineworkers to over one million by 1850.

By 'forward linkages' is meant the opening up through the laying of railines, of hitherto inaccessible hinterlands of continents and therefore access to their resources of minerals, forests and raw materials; and the opening up of new markets among colonised peoples so far insulated from western trade by their remoteness. Since Britain was both the capital-surplus country and the 'workshop of the world' at this time, these many thousands of miles of railways in three continents were financed by British capital lent to governments usually only at a guaranteed rate of return, built by British engineers and contractors who made a lot of money out of their monopoly, and using British-manufactured steel rails, rolling stock and locomotives, which gave an assured outlet for the British capital goods and engineering industries. Given that world railway mileage rose more than twenty times between the decade of the forties and that of the seventies, the stimulus to the British economy may be imagined.

The increase in British investment abroad up to the 1870's, thus brought in its train, owing to the linkage effects, increase in the exports of capital goods, access to cheaper raw materials, and wider access to markets.

Table 16.1 : Increase in World Railway Mileage

	UK	Continent	USA	Rest of World
1840-50	6,000	7,000	7,000	—
1870-80	17,000	73,000	106,000	20,000

16.2.2 The Country Destination of Capital Exports

Most of the capital exports from Britain in the 19th century went either to the European Continent, to the USA and Canada, or to the developing temperate areas of the world where European emigrants had appropriated land and other resources from the original inhabitants, and settled themselves. These included both politically independent regions like N. America, Argentina and Brazil, and the dependent white settler dominions like South Africa and Australia. Very little of British capital exports went to the tropical colonies like India, Malaya or the W. Indies where there were no permanent settlers from Britain. This fact has misled some economists and historians into thinking that the tropical colonies had little role in capital exports from Britain. Actually while they did not receive British capital in any quantity, the tropical colonies did have a very important role in earning foreign exchange through their export surpluses, which Britain took for its own use to avoid balance of payments difficulties vis a vis the countries to which it was exporting capital. This is the mechanism we will examine below in Sub-section 16.3.3.

On the eve of the First World War, of the total holdings by Britain of capital abroad amounting to 3,780 m. pounds, only 380 m. pounds or just over 10% was invested in India and Ceylon. The white settler countries within the Empire (Canada, Australia and N. Zealand, S. Africa) accounted for 1,400 m. pounds while the remaining 2,000 m. pounds which made up over half of the total holdings, were invested in the non-empire regions (the Continent, USA, and S. America). This led Ragner Nurkse to argue in an influential article (*International Investment today in the Light of Historical Experience*) that the predominance of the independent temperate regions in total capital holdings showed that the colonies were no longer important in the age of capital exports. This argument however is a somewhat fallacious one as we will see.

Check Your Progress 1

1) Why could not effective demand increase at a fast pace in the 19th century Britain?

.....
.....
.....
.....

2) Explain the terms 'backward linkage' and 'forward linkage'.

.....
.....
.....
.....

3) Mention the countries which witnessed an inflow of British capital.

.....
.....
.....
.....

16.3 THE ERA OF IMPERIALISM AND OVERSEAS INVESTMENT

In this section, we will discuss how it was possible for colonising countries like UK to combine negative current account balance with a negative capital account balance (i.e. net capital exports) to the developing areas of the world. This question will be related to the continuation of transfers from the colonies.

16.3.1 Imperialism and its Link with Investment

By the second half of the 19th century, Britain was facing the emerging challenge of the later industrialisers in Europe and N. America. Particularly important was the competition from the USA and from Germany, both forging ahead rapidly behind protective tariff barriers in building up their own manufacturing capacity. In both these countries there was a rapid growth of monopolies and of cartels. This took place partly through the faster growth of the larger firms and partly through take-overs and mergers especially at times of recession. In Britain as well, the earlier era of competition between large numbers of firms was giving way over time to oligopolistic conditions in many industries, with a few firms dominating each industry. The monopolies and the association of firms known as cartels, fixed prices and restricted output when necessary to maintain profits. From the 1870's to the First World War, there was a veritable race among the white nations for the seizure of the remaining uncolonised parts of the tropical and semi-tropical world. Britain as the first industrial nation and the most vigorous coloniser, had an unbeatable lead over the others. The more recent industrialising nations, each scrambled to grab territory where it could, before their rivals got there. By 1913 the following countries had substantial colonial possessions whereas they had none in 1870: Germany, USA, and Japan.

While the colonies of all the industrial powers taken together accounted for a total colonised population of 273.8 m: in 1874, this had increased to 523.4 m. by 1913. Over the same period the area in colonised territories had risen from 40.4 m. sq. km. to 65.0 m. sq. km. We will not go into the complex motives behind this rush to

partition the world, except to note that while the economic motive was certainly predominant, there were some cases—such as the grabbing of deserts of both the hot and cold varieties (as in the Sahara and in Alaska) where no immediate economic gain was visible, and the main idea seemed to be to get there before someone else got there first. Of course, some of these acquisitions later turned out to be very valuable.

There was a long period of relative depression in Europe from 1873 to 1895 which is referred to as the 'great depression'. Prices showed a downward trend (despite cartelisation) and there was a profits-squeeze, although no persistently high levels of unemployment were observed, unlike the other later great depression of the 20th century inter-war period. The frenetic scramble to acquire new colonial territories and to complete the partitioning of the world was related to this fall in profitability in domestic markets. Liberal English analysts like J.A. Hobson, author of the well-known book *Imperialism*, were opposed to Britain's overseas expansion and saw it to be the result of a highly inegalitarian social structure at home, which limited the consumption of workers and made overseas investment attractive.

16.3.2 The Colonial Financing of Overseas Investment

Between 1870 and 1914, the two largest single areas of British capital exports were Continental Europe and the USA. Countries were on fixed exchange rates at that time, with the external value of the major currencies being denominated in gold and hence bearing a fixed relationship to each other. (Most European countries were moving out of the silver standard and formally onto the gold standard in the 1870's.) Under such a system, if the balance of payments of a country is in deficit, the deficit had to be settled through the outflow of gold. Since no country could keep unlimited reserves of gold, persistent deficits in the overall balance of payments of a country would cause serious problems.

The peculiar feature of the destination of British capital exports was that it was flowing to precisely those developing, industrialising regions of the world where rates of return to investment were high, but where Britain had no surplus on the current account of its balance of payments to finance these capital flows. To understand what this means you should be first clear about the fact that 'capital exports' are a **debit** item on the balance of payments accounts of the country exporting capital. (It is helpful to think of investment abroad, that is capital exports, as the 'import of IOU's' as Samuelson puts it.) So net capital exports, that is a deficit on the capital account, to a region like the Continent from Britain was possible without causing payments imbalance only if Britain had an offsetting surplus on the current account with these regions to the same extent (remember that the current account is the balance of trade in goods plus in services, plus net transfers). But far from having a current account surplus, Britain in fact had large and increasing current account deficits vis a vis both the Continent and the USA, owing to the fact that Britain's imports of primary products from these regions was rising fast while its exports faced tariff barriers. (Britain's net invisibles earnings balance was positive but not enough to offset its negative trade balance vis a vis these regions, so the deficit on current account tended to widen.)

So, the question arises, given its rising current account deficits, how did Britain carry on investing capital in these regions (that is incurring additionally capital account deficits), and thus increasing the overall deficit on its balance of payments, without being drained of its gold reserves? This is a question that standard textbooks of British economic history never ask.

Thus, in 1880, Britain had a trade plus bullion deficit with Europe of 40.5 m. pounds, and a similar deficit with USA of 64.9 m. pounds. Net invisibles earnings from these regions are estimated at 35 m. pounds at most, giving an overall balance of payments deficit of 70.4 m. pounds, amounting to 16% of GDP.

Table 16.2: UK balance of payments in 1880

Trade plus Bullion Balance of UK in 1880	million pounds
Continent	- 40.5
USA	- 64.9
Total	- 105.4
Less Invisibles balance	35.0
	- 70.4

The Colonial Financing
of Capital Exports in
the 19th Century and some
Theories of Capitalism
and Underdevelopment

The source of these estimates is S.B. Saul, *Studies in British Overseas Trade*. The author points out that Britain had positive balance of payments position vis a vis a number of colonial territories, the most important being India which alone earned 25 m. pounds through its export surplus earnings mainly to the Continent and USA. These export earnings could be taken over by Britain by imposing charges on the Indian revenues to roughly the same amount under various heads of invisibles, charges which were payable in sterling and which derived directly from India's colonial position. In short India's export surplus earnings were used to offset Britain's own deficits and a similar procedure was followed with other colonies. As Saul puts it, 'the position was that Britain settled more than one-third of her deficits with Europe and USA through India'. It suited Britain that India should export to other countries because the exchange earnings were under Britain's control anyway, and Indian goods along with other colonial countries' goods were relatively free of tariff barriers whereas British goods were not. Thus in 1905, India could export without her goods being subject to duty in foreign markets, to the extent of all her exports to Belgium, three fifths of her exports to Germany, over half to the US and 70 per cent to Australia. Colonial exports were a way of Britain jumping tariff barriers. This mechanism was of course far from clear to contemporary governments, or they might have put tariff barriers against more Indian goods; on the other hand, they might not have done so, because these were mainly industrial raw materials which they needed and which could not be produced in temperate areas.

This situation continued for decades. The charges imposed by Britain on the tropical colonies usually somewhat exceeded what they earned by way of their large export surplus, so the colonies were obliged to borrow capital to balance their payments. In the modern world of independent nation-states, it would be unthinkable for a country with as large an export surplus compared to its GDP as India had, to be unable to either build up reserves or invest abroad, but be on the contrary obliged to import capital itself. Japan today has a large trade surplus and invests abroad while the USA has a large trade deficit and is obliged to borrow. In the looking-glass world of colonial trade involving transfers, however, it was the colonised country with the large trade surplus which was obliged to borrow capital, and the metropolitan country with the large trade deficit which invested profitably abroad. This is because the export surplus earnings of the colonies were transferred to Britain. Of course, it is not theoretically recognised as a transfer by the historians of the colonising countries to this day.

By 1910-11, Britain's deficit on trade plus bullion plus invisibles account had widened to between 90 and 95 m. pounds with the Continent and US combined and there was another 32 m. pounds total deficit on merchandise plus bullion account with a number of other countries taken together (Argentina, Australia, Brazil and Canada being the main ones). Yet these were all developing regions where Britain was investing capital, thus moving her overall balance of payments with these countries into even larger deficit. India by its transfer via export surplus, continued to be the largest single earner of foreign exchange for Britain, with a trade surplus in 1911 totalling over 70 m. pounds of which over 30 m. pounds was with the Continent. As regards the U.S., 'India contributed to Britain's dollar settlements by exporting jute and jute goods to the U.S. to a value of over 10m. pounds, something Dundee by its own admission could not have done.... It was mainly through India that Britain's balance of payments found the flexibility essential to a great capital exporting nation' (Saul).

In fact, it is arguable that the question is not simply one of flexibility; that without the colonial transfer to finance her capital exports to areas where she had current account deficits, Britain could not have emerged as a 'great capital exporting nation' at all. At the very least she would have been forced to abandon the gold standard fifty years before she actually did, because she would have faced the alternatives of either not investing in these profitable regions, or being drained of her gold reserves in order to pay for her increasing deficits.

Check Your Progress 2

- 1) How did Britain respond to the falling rate of profit in her domestic production? Why?

.....
.....
.....
.....
.....
.....

- 2) How could Britain invest abroad, in other words, be a net exporter of capital in spite of having a deficit in her current account of balance of payments?

.....
.....
.....
.....
.....

- 3) Do you consider that the 'transfer' from colonies to Britain constituted a drain of wealth for the colonies? How do the historians of colonising countries look at the question of 'transfer'?

.....
.....
.....
.....
.....

16.4 SOME THEORIES OF CAPITALISM AND UNDERDEVELOPMENT

There is a vast literature on the problem of the historical evolution of the relation between today's industrially advanced countries and today's backward or underdeveloped countries. The latter have emerged into political independence from colonised subordinate status, only two to four decades ago.

The question for discussion is, whether their underdevelopment is independent of the historical development of Europe, or a consequence of that development. The adherents of either viewpoint differ in turn on the specific nature of the interaction. In the short space available here we cannot go into the details and complexities of

different theories, but only pick up the salient ideas of some alternative approaches to the question as represented by selected authors.

16.4.1 Linear Development Theories: Rostow and Hicks

- a) W.W. Rostow *The Stages of Economic Growth*
- b) J.R. Hicks *A Theory of Economic History*

In this sub-section we will briefly consider the theories of two authors who while they differ in details, broadly share the perspective of what might be called 'linear development'. By this term we mean the idea that all countries follow a more or less similar sequence of development over time, but differ only in that at any given point of time, some are higher up on the ladder while others are lower down. There is also an implicit assumption, that the fact some countries are very much lower down the ladder, is not related in any way to the fact that others are very much higher up. (By an 'implicit assumption', is meant an assumption that is not openly stated but seems to underlie other statements.)

W.W. Rostow put forward these ideas in *The Stages of Economic Growth*, where he argued that there are five stages of development that every country follows. The most important stage in his five-stage scheme is the middle one, the third stage defined as one of 'take-off into sustained growth'. Although it is given a different name, in substance it does not seem to be different from Industrial Revolution. There are two stages preceding this stage of 'take-off', and two stages succeeding it. The two preceding stages are: the stage of **traditional economy** and the stage of **preconditions to the take-off**. The very first stage of traditional economy, refers to the various types of premodern economic and social structures which are not conducive to modern growth. The stage of preconditions is defined as one of variable duration when the institutional and political changes essential for modernisation take place such as the formation of a nation state and laying down of minimum infrastructure.

Rostow specifies the following features of the 'take-off' stage: a) 'a rise in the proportion of net investment to national income from say 5% to over 10%, definitely; outstripping the likely population pressure and yielding a distinct rise in output per capita', b) the development of one or more substantial manufacturing sectors with a high rate of growth, which might be called 'leading sector/s', c) the existence or rapid emergence of a political, social and institutional framework which promotes growth.

Certain tentative dates or rather periods are identified by Rostow when the 'take-off' took place in different countries:

Table 16.3: Country take-off periods as identified by Rostow

Country	Period	Country	Period
UK	1783-1802	CANADA	1896-1914
FRANCE	1830-1860	RUSSIA	1900-1914
USA	1843-1860	ARGENTINA	1935-
GERMANY	1850-1873	TURKEY	1937-
JAPAN	1878-1900	CHINA	1952-
		INDIA	1952-

The criticism of Rostow's theory has been at two levels: the first at a fundamental level of methodology, put forward in a review article on the book, by P. Baran and P. Sweezy. These authors argued that the theory specified no mechanism of transition from one stage to another, and therefore did not contain any genuine theory of dynamics in history. The 'preconditions' stage for example could only be identified negatively, as contrasted with that of industrialisation; the latter, the stage of 'take-off' similarly could only be identified *ex post* after industrialisation had taken place but could not be predicted on the basis of anything in the theory. The theory was thus not a theory at all but mere description, and not accurate even as description.

Other economic historians have criticised Rostow on the basis of non-fulfilment of

the empirical criteria he had laid down. Habakkuk and Deane argued that the stage identified as the 'take-off' in Britain did not see a doubling of the rate of net investment to national income even over a much longer period than the one specified, and this was endorsed by K. Berrill. You will be able to add another important if obvious criticism yourself: the theory ignores the historical reality of colonialism and imperialism completely. It assumes away the interaction which existed over many centuries between the advanced industrial countries and today's ex-colonial underdeveloped countries. As a result of this Rostow puts forward a unilinear conception of historical development in which all countries pass through the same five stages and differ only in that some do so later than others.

Although writing from a somewhat different perspective J.R. Hicks in a short monograph, *A Theory of Economic History* also adheres to the same unilinear conception for the same reason, a complete ignoring of colonialism and imperialism. Hicks uses the term 'revenue economy' to denote the systems preceding capitalism. He argues that the 'rise of the Market' namely the growth of trade leads to a transition to Capitalism, and since certain countries by their location — such as those bordering the Mediterranean — were particularly well placed to develop trade, they saw an earlier growth of Capitalism. Thus, there is a strong geographical element to the theory. Hicks assumes that the countries which saw the 'rise of the Market' went on to industrialise.

However, economic historians like Maurice Dobb have pointed out that the growth of trade, was not synonymous with the growth of capitalist production. It could be equally compatible with the growth of slave-based export oriented production as happened in Antiquity, or with the intensification of labour services as happened in the 16th century in E. Europe. In the 17th and 18th century the highly market-oriented colonising, industrialising nations in fact revived slave-based plantations. Thus, the 'rise of the Market' by itself can explain very little regarding capitalist production. Secondly, the countries in Europe which were foremost in trade in the 16th and 17th centuries such as Italy, Spain and Portugal, were not the first to pioneer Industrial Revolution.

16.4.2 Colonies Viewed as a Capitalist Periphery

Here we will consider the ideas of A. Gunder Frank, as the representative of a large school of writers in the L. American context. Unlike the authors considered earlier, Frank puts the historical relation between the colonies and dependent countries on the one hand, and the industrialising countries of Europe, at the centre of his analysis. The latter is called the 'metropolis' in relation to the former, which make up the 'satellite' countries of the 'periphery'. He is categorical in stating that from the beginning of this relation there was the promotion of exports and through this avenue the transfer of economic surplus took place from the satellite countries to the metropolitan countries. Development in the metropolitan countries produced underdevelopment in the satellite countries, and Frank is at pains to stress that underdevelopment is to be looked upon not as a state, but as a process which is historically related to industrialisation in the metropolis.

So far you might find little to disagree with in this theory. However, Frank and his school (which include Samir Amin and Emmanuel Wallerstein) go on to say also that from the beginning of the metropolis-satellite relation, the system of production in the satellite countries was capitalist in character. Either capitalist relations were instituted by the colonisers wherever they settled, as in L. America; or, existing relations were altered in the direction of capitalism as, he argues, in India when the British instituted the *zamindari* system. Now systems like *zamindari* are in fact identified by us in India with feudal relations since they involved extraction of high rates of rent from a mass of small producers. In Frank's view however the colonised and dependent countries lack all claim to any economic and social structure which is in any way autonomous of the structure of the metropolis; further, there is a certain similarity with Hicks's view in that Frank explicitly states that production for

the export market necessarily implies that production is capitalist. He therefore characterises every export-oriented colony or satellite as being capitalist and as constituting the periphery of the world capitalist system.

Particularly for Asian countries like India or China with their long social history and highly articulated class systems at the time of the European impact, this view clearly constituted a severe oversimplification. It represents a Euro-centric view which sees the economy of the underdeveloped countries entirely as the creations of the Europeans. Further, we find that the same familiar fallacy is repeated, of identifying production for the market with capitalist production. In reality the European impact of promoting commercialisation had to operate necessarily through the existing socio-economic structures. And it did not necessarily require the reproduction of capitalist relations in the colonies to ensure the transfer of surplus.

16.4.3 Colonies Viewed as Markets

One of the most interesting and complex theories of colonialism is that advanced by Rosa Luxemburg, in *The Accumulation of Capital*. This book is the only attempt to argue at the level of economic theory, that without external markets including colonial markets, industrialisation under capitalism cannot take place. While many authors had described the working of colonialism, none had integrated colonial exploitation into the theory of capitalist accumulation itself.

Rosa Luxemburg argued that there was a logical contradiction in saying that accumulation (that is, continuous reinvestment of capital, and output growth) could take place within a closed capitalist system consisting only of the two classes of capitalists and workers. This was because the total social product in such a system consisted of wages and profits. (It is useful to remember that about half of the social product was wages going to perhaps 90% of the population while the remaining half was profits and rents going to perhaps 10% of the population.) While the workers consumed what they got as wages, the capitalists could consume only a tiny part of their profits, and had to reinvest the rest. However, the problem was, who was to consume the increased product arising from reinvestment? And why should there be any incentive for capitalists to reinvest at all unless they could be assured of a market for their products?

Thus the argument Luxemburg advanced was that external markets were a logical necessity for the capitalist production system to be able to exist and function as a capitalist system: that accumulation within a closed capitalist economy was a logical impossibility. Her conception of 'external markets' included all the strata of small producers like peasants and artisans who were initially outside the framework of capitalist production. At first the capitalist sector converted these strata within the boundaries of the national economy, into its labour force and at the same time its markets, by destroying the basis of independent small production through measures like the 'enclosures' in agriculture. Once this source was exhausted the same process was extended to peasants and artisans in subordinate countries outside the national economic boundaries: their petty production was destroyed through unrestricted inflow of factory produced goods and the petty producers were converted over time to hired workers constituting a market for the capitalist sector of the industrial country. Colonialism was thus seen by Luxemburg as a necessity for the functioning of the advanced capitalist economies, and she was able to integrate colonial exploitation into the analysis of capitalism. In her concept of 'external markets' Rosa Luxemburg also included such modern ideas as unproductive military spending.

Check Your Progress 3

- 1) Why can you not consider Rostow's linear development theory as a theory?

.....

.....
.....
.....
2) Why is Rostow's 'theory' described as a 'linear' development theory?

.....
.....
.....

3) Provide a brief critique of Hicks's theory of economic history.

.....
.....
.....
.....
.....

4) Distinguish between a satellite and a metropolis.

.....
.....
.....
.....

5) Was the colonial Indian economy a capitalist one? Justify your answer.

.....
.....
.....
.....

6) Why according to Luxemburg, do the industrialised countries colonise underdeveloped economies?

.....
.....
.....
.....
.....

16.5 LET US SUM UP

In this Unit you have obtained some idea of the importance of the export of capital for the British economy in the second half of the 19th century. The peculiar feature of this export of capital was that it flowed to the developing areas of the world such as the European Continent, N. America and the white settler dominions where returns were good, but where Britain had increasing current account deficits in most cases. Under the gold standard which involved fixed exchange rates, increasing deficits on her balance of payments would have meant that Britain would have been either drained of its gold reserves or

forced to cease her profitable investments abroad. Neither of these things happened because the large transfer from the tropical colonies in the form of increasing export surplus earnings from these areas, could be utilised by Britain to settle a major part of her own deficits, by imposing various invisible charges on the colonies. It is very doubtful whether profitable capital exports from Britain could have continued without the 'colonial safety valve'.

In the second part of this Unit you have gained some idea of the wide differences in the theoretical approaches to the question of the historical relation between today's advanced industrialising countries and today's ex-colonial developing countries.

16.6 KEY WORDS

Chartism: Workers' movement deriving its name after the People's Charter drawn up in 1835 by the Working Men's Association.

Corn Law: Law passed to ban import of corn by imposing prohibitive tariff so that the farmers and the landed aristocracy benefit at the expense of the urban working class and the industrialists by keeping bread prices high. This law was repealed in 1846 and is seen as a victory for the industrialists.

Metropolis: Term used by Frank to describe the industrialising countries of Europe.

Periphery: Colonies of the 'metropolis'. Their economies were directed according to the interests of the metropolis.

16.7 SOME USEFUL BOOKS

Hicks J.R., 1969. *A Theory of Economic History*, Oxford University Press, London.

Hobsbawm E.J., 1969. *Industry and Empire*, Pelican London.

Hobson J.A., *Imperialism*, George Allen and Unwin, London.

Floud & McCloskey (ed.). *The Economic History of Britain*.

Frank A.G., 1969. *Capitalism and Underdevelopment in Latin America*, Monthly Review Press, New York.

Luxemburg R. 1951. *The Accumulation of Capital* (Routledge); London.

Rostow W.W., 1969. *The Stages of Economic Growth A non-Communist Manifesto*. London; Cambridge University Press.

16.8 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) Read Sub-Section 16.2.1 and answer.
- 2) Read Sub-Section 16.2.1 and answer.
- 3) Read Sub-Section 16.2.2 and answer.

Check Your Progress 2

- 1) Read Sub-Section 16.3.1 and answer.
- 2) Read Sub-Section 16.3.2 and answer.
- 3) Read Sub-Section 16.3.2 and answer.

**Unequal Exchange,
Colonial Transfer and
The Financing of
Industrial Revolution
and Capital Exports**

Check Your Progress 3

- 1) Read Sub-Section 16.4.1 and answer.
- 2) Read Sub-Section 16.4.1 and answer.
- 3) Read Sub-Section 16.4.1 and answer.
- 4) Read Sub-Section 16.4.2 and answer.
- 5) Read Sub-Section 16.4.2 and answer.
- 6) Read Sub-Section 16.4.3 and answer.



UNIT 17 THE CENTRE-PERIPHERY THESIS : THE LATIN AMERICAN SCHOOL

Structure

- 17.0 Objectives
- 17.1 Introduction
- 17.2 Origin of the Thesis
- 17.3 Three Versions or Approaches of Latin American School
 - 17.3.1 The Approach of Frank and dos Santos
 - 17.3.2 The Approach of Sunkel and Furtado
 - 17.3.3 The Approach of Cardoso
- 17.4 The Common Points of the Three Approaches
- 17.5 The Concept of Dualism
 - 17.5.1 Dualism on International Plane
 - 17.5.2 Domestic Dualism
- 17.6 Practical Implications of the Thesis
- 17.7 Limitations of the Thesis
- 17.8 Let Us Sum Up
- 17.9 Key Words
- 17.10 Some Useful Books
- 17.11 Answers/Hints to Check Your Progress Exercises

17.0 OBJECTIVES

This unit aims at introducing you to the approach of a group of leading Latin American economists to the problem of underdevelopment.

After going through this unit, you will be in a position to explain :

- how the economists from underdeveloped countries of Latin America look at the problems and possibilities of development,
- how the Latin American economists bring in the role of imperialism to explain the inability of Third World countries to develop even though they have labour and natural resources,
- how dualism of centre-periphery operate externally and internally and what its implications are, and
- the weaknesses of this approach.

17.1 INTRODUCTION

In previous units, we have read about the development experiences of some important countries of the world, which started their journey on the path of development at different points of time and in different circumstances. The three countries about whom we read were politically independent and not under political or economic control of a foreign power. Hence, when a number of countries became politically independent after the Second World War, they did not have readily

A number of economists from the West argued that the experiences of the developed countries were not only relevant but could be followed. These developed countries were also once backward agricultural societies not much different from the countries of Asia, Africa and Latin America in the 1940s and 1950s. The backward countries of Asia, Africa and Latin America had no shortage of labour and natural resources. What they lacked was capital and technical know-how which could be injected from outside and, then, they could follow the historical experiences of developed countries.

This view was contested by a number of Latin American economists. They termed the Western approach as too simplistic and not in tune with the ground realities. The main hurdle in the way of development of the countries of Asia, Africa, and Latin America was structural and no amount of foreign capital would bring about their economic development. The Western economists ignored the fact that there was a powerful world capitalist system influencing the process of development and trying to keep the backward countries in such a situation that they subserved the latter's interests.

The view point of Latin American economists came to be widely known as the **dependency thesis**.

17.2 ORIGIN OF THE THESIS

The dependency thesis owes its origin to Raul Prebisch, a well-known economist from Argentina. During the 1950s, he headed the Economic Commission for Latin America (ECLA) and in the course of his official duties, he came to acquire certain very useful insights, in the light of which he became the forerunner of dependency thesis which may be called "structuralism". This was in response to the monetarist approach of neo-classical economists. It refuted the argument that the development of underdeveloped countries was solely due to a lack of capital, especially foreign exchange resources.

Prebisch and his colleagues at ECLA realised that import substitution was also not the way out. In fact, the argument in favour of import substitution was advanced because it was found that the exports of primary products were subject to terms of trade which fluctuated widely in the short-run and deteriorated in the long-run. Thus import substitution behind tariff walls was supposed to reduce the dependence of Latin American countries on the USA and other developed countries who charged high prices for manufactures and paid very low prices for primary goods.

Experience showed that the policy of import substitution did reduce the imports of certain finished goods, especially consumer durables, but it necessitated the increased imports of capital goods, raw materials and fuel and led to greater dependence on transnational corporations. The emphasis on industrialisation resulted in more employment opportunities in the industrial sector and greater purchasing power at the disposal of industrial workers. To satisfy the demand of these workers for food items, the recourse to imports had to be taken.

It was realised by Prebisch and his colleagues that import substitution created dangerous forms of dependence for Latin American countries rather than making them economically independent. This realisation converted Prebisch and his colleagues from "structuralists" into "dependency" theorists. They did not give up their earlier theories but shifted the emphasis and added new dimensions. They drew on a very important idea of Raul Prebisch that the world could be divided into two parts. The first part consisted of a "core" of dominant nations or the 'centre' and the other part of a "periphery" of dependent ones.

Dependency theory was influenced and reinforced by Marxist critiques of imperialism. The fundamental contribution of those who were influenced by Marxian thought was that the core or the centre was not favourably disposed towards the

From the middle of the 19th century onwards, export of capital has become the main feature of international economic relations between advanced capitalist countries and the rest of the world. It is the result of rapid rate of accumulation and increasing difficulties in its profitable investment in the home countries. This, along with other factors, has encouraged advanced capitalist countries to look for deployment of investible resources outside their boundaries. Other factors include domestic problems of labour discipline, high welfarism, relatively lower rates of profit, etc. Obviously, monopoly capitalism is more expansive and outwardly aggressive than competitive capitalism of the earlier phase.

It follows from this that the relationship between the centre and the periphery is, because of the very nature of the structural needs of the centre, bound to be exploitative. Their interests are mutually antagonistic and incompatible. As more and more surplus is extracted from the periphery in various ways and transferred to the centre, the problem of absorption of this increasing surplus gets aggravated and leads to more aggressive outward expansion by the centre. Obviously, the countries of Asia, Africa and Latin America are caught in the vicious trap of the centre. They are exploited to extract and drain away maximum possible surplus and then the problem of surplus-absorption is to be solved at their expense. This makes economic development of underdeveloped countries an impossibility so long as the centre-periphery nexus is not broken.

Check Your Progress 1

- 1) Mark (T) for True and (F) for False statements.
 - a) Western economists argued that the historical experience of the developed countries cannot be followed for the development of backward countries.
 - b) Latin American Economists argued that the main hurdle in the development of backward countries was lack of capital and technical know-how.
 - c) According to Prebisch, import substitution was the only way out for backward countries.
 - d) The vicious trap of centre and periphery has made economic development of less developed countries almost impossible.

- 2) Briefly describe the background of dependency thesis. (Answer in 100 words)

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

- 3) Explain the term "Centre" and "Periphery" and the relations between them. (Answer in six sentences)

.....

.....

.....

.....

.....

17.3 THREE VERSIONS OR APPROACHES OF LATIN AMERICAN SCHOOL

There are three important versions of dependency thesis, given by Latin American economists. We shall underline only the differences among them before we go on to discuss each one of them separately.

The first version is from Andre Gunder Frank and Theotonio dos Santos. Their main distinguishing feature is that, they deny the possibility of capitalist development in the periphery. What can happen is only the "development of underdevelopment".

The second version, given by O. Sunkel and Celso Furtado, does not deny the possibility of capitalist development in the periphery provided the hurdles in its way are cleared. Among the hurdles market constrictions are very important.

The third version is by Fernando Henrique Cardoso. It accepts the possibility of capitalist development in the periphery, but it will be subservient to the capitalism of the centre.

We have mentioned the names of only the most important proponents of the three versions of dependency thesis from the Latin American school of economists. Another thing needs to be noted here is that the differences that divide dependency thesis go farther than differences regarding only the possibility of development within the world capitalist system in the countries of Asia, Africa and Latin America.

17.3.1 The Approach of Frank and dos Santos

As has already been mentioned, Andre Gunder Frank and Theotonio dos Santos have been important dependency thesis proponents. They began from where the American economist Paul A. Baran left. Baran in his book *Political Economy of Growth* tried to show that economic development of underdeveloped countries was not in the interest of advanced capitalist countries. As has been already mentioned, economic development in underdeveloped countries will close down important sources of raw materials and natural resources and the market for finished goods for advanced capitalist countries. The problem of absorption of surplus capital of advanced capitalist countries will become aggravated.

To prevent the possibility of economic development in underdeveloped countries, advanced capitalist countries will form alliances with pre-capitalist domestic elites like feudal, tribal and semi-feudal strata of underdeveloped countries. These strata are also hostile to capitalist development because they will be adversely affected. The alliance will try its best to stop capitalist transformation in underdeveloped countries, so that the advanced capitalist countries continue to have **uninterrupted access** to the resources of underdeveloped countries and maintain traditional modes of surplus extraction. Thus the possibilities of economic growth in dependent countries will be extremely limited. They will always remain starved of capital for investment in the sectors and areas given higher priorities in the national interest. The surplus generated by them would be largely expropriated by foreign capital and the rest would be squandered on luxury consumption by traditional elites. Whatever little capital and foreign exchange resources would be mobilised by underdeveloped countries, their multiplier effects would benefit advanced capitalist nations because capital goods such as machinery, equipment, etc. would have to be bought from them.

Thus, there is no escape from this trap. The only way out is political change. Underdeveloped countries, desirous of having their own independent economies, must opt out of the world capitalist system.

Starting from this point, Andre Gunder Frank tries to develop the thesis that the only political solution is a revolution of socialist nature because so long as an underdeveloped country remains a part of the world capitalist system, there cannot be any alternative to its underdevelopment.

There are three levels in Frank's analysis of dependency as a theory of underdevelopment.

At the first level, Frank tries to demonstrate that large areas in the periphery have been incorporated into the world economy since the early days of colonialism. At the second level, he endeavours to show that such incorporation into the world economy has transformed the countries of the periphery into capitalist economies. At the third level, Frank tries to prove that the integration of these supposedly capitalist economies into the world economy achieved through an interminable satellite chain in which the surplus generated at each stage is successively drawn off towards the centre.

According to Frank, so long as this satellite-metropolis arrangement exists, there is no real possibility of sustained development of the countries of the periphery. This arrangement of things can weaken as a result of exogenous factors. There are only two options open to satellite countries: breaking completely away with the metropolis-satellite network through a socialist revolution or continue to "underdevelop" within it.

Frank holds that no country was ever in the state of "underdevelopment", it might have been "undeveloped". Underdevelopment is the consequence of the world-wide mercantilist and capitalist expansion of European nations. Developing metropolises and underdeveloping satellites emerged and all parts of the world from metropolitan centres in Europe and later USA to farthest outpost in the the Latin American countryside got linked up. This arrangement has worked largely to the advantage of the metropolis, but there are instances to show that some satellites also have economic development, but they are in the category of exceptions and they have been termed as "submetropolises".

An important aspect of Frank's analysis is his rejection of the assertion that underdeveloped countries suffer, to a great extent, from their dualistic societies. It is claimed that the main hindrance in the way of their economic development is that underdeveloped society is dualistic — one part is modern, urban, and integrated while the other part is rural, backward, and isolated and feudal in character. This latter part is not integrated with the metropolis.

In fact, evident inequalities in income and differences in culture have led people in certain quarters to assert the existence of "dual" societies and economies in underdeveloped countries. They claim that each of the two parts has a history of its own, a structure and dynamics largely independent of the other. Only one part of the economy and society is supposed to have been affected by relations with external capitalist world and, as a result, has become modern, capitalist, and relatively developed while the other part is still isolated, subsistence-oriented, pre-capitalist and, therefore, underdeveloped.

Frank calls the entire "dual society" thesis false and the policy prescriptions based on it will intensify and perpetuate conditions of underdevelopment. History shows that the expansion of the capitalist system over the past centuries, has effectively and entirely penetrated even the apparently most isolated sectors of the underdeveloped world. The so called backward or feudal domestic areas of an underdeveloped country are no less the products of the single historical process of capitalist development than are the modern sectors. Thus underdevelopment is not due to the survival of pre-capitalist institutions and a lack of capital in areas that have remained isolated from the mainstream of development. On the contrary, underdevelopment was and still is generated by the very same historical process which also generated economic development : the development of capitalism itself. This connection has not automatically brought about capitalist economic development. In spite of the participation of these countries in world trade and division of labour, what has

Theotonio dos Santos regards dependence as a conditioning situation in which the economies of one group of countries are conditioned by the development and expansion of others. A relationship of interdependence between two or more economies or between such economies and the world trading system becomes a dependent relationship when some countries can expand through self-impulsion while others who are in a dependent position can only expand as a reflection in the dominant countries.

T. dos Santos rejects the Western as well as socialist model of development as not applicable to Latin America. According to him, the Western or capitalist model is based on the assumption that all underdeveloped countries of the world have to follow, in essence, the path traversed by the USA, Europe and Japan. They can start their journey towards building a modern or industrial society as soon as they succeed in eliminating the obstacles created by pre-capitalist societies and their vestiges.

T. dos Santos terms the capitalist model as ahistorical and formal. It is wrong to say that underdeveloped countries are bound to repeat the experiences of developed ones and build a society resembling the existing developed society of the west. He asserts: "Historical time is not unilinear and future societies will not be able to attain stages reached by other societies at a previous time." Underdeveloped countries are in a completely different situation as compared to developed countries when they start the process of industrialisation. The former do not have their basic sources of private capital formation in foreign trade, the incorporation of vast masses of workers in industrial production, their indigenous technological development and a colonial system. The capitalist model has been based on "socialism in one country (or bloc)", "primitive socialist accumulation" at the expense of peasantry and handicrafts, autarchy along with an iron curtain and the primacy to basic and heavy industries. This course is also not open to Latin America.

Hence, the need is to look into the concrete historical situation and conditions of an underdeveloped country before prescribing what path or course of development it should take. From this point of view, Latin America is a region where underdevelopment has arisen as a result of the survival of a feudal economy and society along with an export-based and monoculture economy. During the nineteenth century, its economy became outward-oriented, exporting primary goods and importing manufactured products. Socio-economic inequalities widened, on the one hand, while on the other, industrial, technological and institutional backwardness continued. And the economy became dependent on foreign trade and subject to fluctuations in terms of trade. As an alternative to this, inward-oriented development strategy based on import-substitution was tried, but dependence did not lessen. The combination of import substitution and currency devaluation could not lessen dependence on foreign trade. In fact, neither export earnings could increase nor did import bill decline. During outward-oriented phase imported products were generally luxury goods and their effects on the economy were not very decisive. But when import-substitution was emphasised, luxury goods import was drastically reduced and foreign exchange was used to import machinery, equipment and other inputs for setting up and running national industries. In this situation, the availability of foreign exchange became a limiting factor. Latin American countries became dependent on those who controlled the world market and technology and the sources of foreign exchange. Declining prices of primary products and rising prices of manufactured products along with increasing freight charges, royalties, interest rates, etc. led to increasing balance of payments problem and indebtedness. The control of Latin American economies remained effectively in the hands of MNCs. Since there was no socio-economic structural reform of the economy, the pattern of production remained oriented to the elite. The problem of unemployment became more acute because the technology was capital-intensive.

According to dos Santos, the Latin American situation can be understood only with the help of dependence hypothesis. International relationships which condition development can be defined as relationships of dependence. Development emerged as a world-wide historical phenomenon as a result of the formation, expansion and consolidation of the capitalist system. Both the developed countries and others who

came into existence. It is the interest of developed capitalist countries to align themselves with the forces in underdeveloped countries that preserves the latter's backwardness. Dependency hypothesis does not concern itself with an analysis of underdevelopment simply in terms of certain isolated pre-capitalist structures, but tries to approach it in the context of the development of capitalism. Obviously, the countries which grow up in the situation of dependency and within the process of capitalist expansion are capitalist. It is not correct to say that their underdevelopment is due to feudalism. In the words of dos Santos : "The capitalist system arises like a central star which exploits an entire system of satellites and sub-satellites which in their turn exploit those lower down in the system. Within underdeveloped countries, therefore, we find a system of internal exploitation linked to the international system."

17.3.2 The Approach of Sunkel and Furtado

Oswaldo Sunkel has combined the ECLA point of view with that of the people who focussed attention on internal constraints. As has already been mentioned (see Section 17.2) that the economists of the ECLA had attempted to explain the phenomenon of Latin American underdevelopment in terms of the pattern of foreign trade of Latin American countries. They were exporters of primary goods and importers of manufactured products, and the terms of trade were always unfavourable to them. They called for determined efforts to bring in diversification in the export trade and accelerate industrialisation through import substitution. This model failed to achieve the desired results. It was thought that its failure and the mess created by it were due to internal constraints to industrialisation. These internal constraints included existing land relations and other institutional arrangements. Sunkel combined the external factors with internal constraints to development in order to present his own approach.

Thus, Sunkel, like Frank and dos Santos, holds that the unit of analysis in studying underdevelopment cannot be the national society. Domestic cultural and institutional factors of a Latin American country are not the key variables responsible for its backwardness though they have an important bearing. The phenomenon of underdevelopment or backwardness can be understood only with reference to the development of capitalist system on the world scale and the place of this particular country in it. The world capitalist system is characterised by the unequal but combined development of its different components. Both underdevelopment and development are integral aspects of the same phenomenon and are historically simultaneous and one cannot exist without the other. They interact and condition each other. Industrial countries become central while underdeveloped, backward countries become peripheral. The centre is the main beneficiary of development because it alone has the dynamism while the periphery also receives some benefits.

Obviously, Sunkel believes that development in Latin America is possible provided the internal constraints are removed and industrialisation based on import substitution and export diversification is pursued. His approach is not pessimistic like that of Frank and dos Santos.

Celso Furtado too believes that the phenomenon of underdevelopment is the consequence of the development of capitalism as a world system. In Latin America, it created hybrid structures, one part tending to behave as capitalist while the other perpetuating the features of precapitalist system. Whether the capitalistic penetration in a country of Latin America will induce industrialisation and development, will depend basically on the quantum of income generated and available to the community. To recall, in such a country an export sector comes into being in order to cater to the demands of developed countries.

Experience shows that the economic structure of such a country does not undergo any big change as a result of this capitalist penetration.

There is no appreciable increase in the absorption of labour and the wages have no relationship with the level of productivity. Obviously, capitalist penetration does not lead to any dynamism in the economy and society and the profits generated by it are not used for productive purposes in it

In most of the countries which became export-oriented, "external demand" became a crucial factor. If the external demand increases along side the improvement in prices of export goods, the profits of the enterprises engaged in their production and export increases. In the course of time, the relative importance of subsistence sector declines. There arises a possibility of growth. This can be realised provided there are reforms to remove internal constraints and currency devaluation to increase exports and there is import substitution. A higher stage in underdevelopment is reached when the industrial nucleus is diversified and is in a position to produce capital goods needed for expansion of productive capacity. This will give a big boost to the process of growth. Thus, Celso Furtado holds that underdevelopment is not a necessary stage in the process of formation of capitalist economies. It occurs because of the penetration of modern capitalistic enterprises into traditional or precapitalist structures. Furtado does not believe that Latin American development is not possible without the defeat of world capitalism. He is optimistic.

17.3.3 The Approach of Cardoso

Fernando Henrique Cardoso has adopted a different approach. He disagrees with Frank, dos Santos, Sunkel and Furtado. He rejects the view that capitalist development is impossible in Latin America unless it goes out of the orbit of the world capitalist system. Second, he does not accept the view of dependent capitalism based on the extensive exploitation of labour, and labour has to be paid only subsistence wage. Third, he regards it erroneous that native or national bourgeoisie in Latin American countries is no longer an active social force but a parasitic class. He criticises the view that the penetration of multinational corporations into Latin American countries have led to the development of "sub-imperialism" and that states in those countries pursue policies that are expansionist. Last, it is not correct to say that Latin America is standing at the cross-roads and there are only two options open to it – if it chooses to remain within the world capitalist system, it has to become fascist or if it opts out of the world capitalist system, it can pursue the socialist path of development which will benefit the masses.

Cardoso thus comes to the conclusion that development is possible in Latin American countries with the help of national capitalist class which is not totally subservient to developed capitalist countries and their multinational corporations. It needs to be underlined that relations of dependency are handy to explain the historical roots of underdevelopment in Latin America, but it does not follow from it that dependent relations by themselves perpetuate in all cases the situation of underdevelopment. Cardoso, on the basis of his study of contemporary Brazil, underlines the possibility of development. It is a different matter that this may be "associated-dependent development".

17.4 THE COMMON POINTS OF THREE APPROACHES

In spite of many differences, there are a number of common points in the three approaches. First, dependency theory alone can explain the historical roots of backwardness or underdevelopment of Latin American countries. Second, underdevelopment is not the original state of existence. In fact, underdevelopment has been caused by the development of capitalism in the West and the integration of Latin American countries in the world capitalist system. Third, as a result of the emergence of developed capitalist countries, some sort of dualism came into existence – the developed capitalist countries became the centre of development while underdeveloped countries became the periphery. Last, import substitution by itself cannot generate the process of development in Latin America. In fact, it may lead to greater dependence and bigger crisis.

Check Your Progress 2

1) Underdevelopment is a natural outcome of the world capitalist system. Explain

17.5.1 Dualism on International Plane

As a result of the emergence of capitalism and its development, the world got divided into two parts, developed and underdeveloped or the centre and the periphery. The interrelations between the two are such that the rapid growth of the former are marginally helpful to the latter. In fact, it pushes the latter further downwards. There are a number of forces, perpetuating international dominance and dependence :

- a) The capacity of developed capitalist countries to control world resources and manipulate commodity markets to their advantage.
- b) Through multinational corporations, foreign investment activities are conducted in order to perpetuate international capitalist domination of the economies of underdeveloped countries.
- c) The developed capitalist countries have greater access to and control over scarce raw materials and natural resources.
- d) The developed capitalist nations have a tight control over latest and sophisticated technology and they export outdated and inappropriate technology to underdeveloped countries under an inequitable patent and licensing system.
- e) The developed countries try to disrupt the efforts of underdeveloped nations at industrialisation by dumping their cheap goods on their markets.
- f) The developed nations adopt harmful trade and aid policies towards underdeveloped countries.
- g) The developed countries lure away skilled and professional people from underdeveloped countries, popularly termed 'brain drain'.
- h) Consumerism and demonstration effect promoted by television, newspapers and magazines and movies prove very harmful to underdeveloped countries and their meagre savings are spent on luxury and other non-essential goods.

17.5.2 Domestic Dualism

Dualism is disruptive of internal economic structure of underdeveloped countries also. There is a glaring gap in income and standard of living of different sections of the society. Per capita income and standard of living vary greatly between the top 20 per cent and bottom 40 per cent of the population. The majority of the people in the top income bracket reside in towns and cities while most of the poor people live in rural areas. Even in the urban areas affluence coexists with slums.

This kind of dualism – the coexistence of "superior" with "inferior" – is not confined only to the distribution of wealth, income and power. In the industrial sector, small enclaves of modern industries based on modern imported capital-intensive technology exist side by side traditional, labour-intensive, small-scale industries, meant for meeting local demands.

The distance between these modern enclaves and traditional activities does not appear to be disappearing but increasing. Likewise the gap between the wealthy elites and masses of poor people shows no sign of disappearing. A large segment of population seems to be barely touched by development. The 'spread effects' of developmental activities have not benefited the lower segments of the society in any appreciable manner. Some people claim that there is a direct relationship between growing affluence of the elites and poverty of the vast masses of people. In other words, affluence is at the expense of the weaker or inferior elements.

It has also been suggested that there is no insoluble contradiction between the elites in the centre and those in the periphery. In fact, both are linked with each other though the elites of the centre curtail the areas of activities of the elites of the periphery.

17.6 PRACTICAL IMPLICATIONS OF THE THESIS

possible so long as the countries of Latin America are a part of the world capitalist system. At best, some sort of dependent-associated growth may take place. Under the centre-periphery thesis, the decision-making is located in the centre and the countries of the periphery have only to follow the dictates of the developed capitalist countries and their multinational corporations are the instruments through which these are implemented. The mobilisation and deployment of resources do not take place keeping in view the needs of the vast majority of the people of the countries of the periphery.

Second, it follows from the above that the countries of the periphery must try to break away with the world capitalist system and end the domination of the local elites. Only after the decision-making shifts to the countries of the periphery, there is any hope of independent economic development. It is not clear how this break can be brought about and who will lead this process. Nothing is clear from the writings of scholars on this point.

Third, since neither the countries of the centre nor those of the periphery are homogeneous or at same stages of development, types of domination and dependence are not the same. The protagonists of the thesis have stated only the general characteristics. In this situation, it is not clear what strategy and tactics the countries of the periphery should follow to free them from the domination of developed capitalist countries.

It seems that apart from the agitational utility, there is not much practical value of the thesis.

17.7 LIMITATIONS OF THE THESIS

The common feature of all the adherents of the thesis is that they hold the 'external forces' domination the main cause for socio-economic backwardness of underdeveloped countries. They try to explain underdevelopment in relation of domination in exchange, that is, trade. They ignore the level of development of forces of production and relations of production in underdeveloped countries. Thus, their thesis suffers from one-sidedness and is incomplete. They talk of the exchange of surplus product of underdeveloped countries and its appropriation by developed countries, but no light is thrown on how it is produced.

They have placed all the emphasis upon the domination of developed countries over backward countries. Among the former, according to their implicit understanding, the USA is so powerful that its writ runs **unchallenged**. May be because of their proximity and historical experience Latin Americans concentrate their attention mainly on the USA but this is not the whole truth. The rivalries among developed countries and the weakening hold of the USA since 1960s have been underlined several times. The capacity of the USA to dominate other developed countries has considerably weakened.

The thesis lacks empirical basis. No scholar has provided data from a number of countries to test the formulations. In fact, it is not capable of being tested because it dwells only on generalities which are, at times, vague.

The thesis is mechanical in nature. It assumes certain things and then proceeds to state that external structures are independent variable while the internal structures are dependent ones. Thus, internal structures do not possess any autonomy and are not capable of breaking out of the orbit of influence of the external structures. In this kind of analysis, there is no place for classes and class relations.

Check Your Progress. 3

- 1) Differentiate between domestic dualism and dualism on international level. Briefly explain the concept of domestic dualism. (Answer in six sentences).
-

.....
.....
.....
.....
.....
.....
.....
.....

2) What are the practical implications of dependency thesis? (Answer in four sentences)

.....
.....
.....
.....
.....
.....
.....

3) What are the limitations of dependency thesis? (Answer in four sentences)

.....
.....
.....
.....
.....
.....
.....

17.8 LET US SUM UP

During the years following the end of the Second World War when the problem of development of the newly independent countries came up in a big way, an attempt was made by Western scholars that underdevelopment was due to their lack of ample savings leading to meagre investment, technological backwardness, low level of education, almost complete absence of infrastructural facilities and so on, besides pre-capitalist institutions and relations of production.

This view was challenged by Latin American economists who contended that underdevelopment was not an original state of existence for newly liberated countries, it was the result of the establishment and development of world capitalist system. Investible surplus was drained away from colonies and they were not allowed to have their independent economic development. They were made to export primary goods and import manufactured products. Thus they became dependent on developed capitalist countries. The Latin American economists divided the countries into two groups : (a) the countries of the Centre, which had developed capitalist economies, and (b) the countries of the Periphery, which included underdeveloped countries.

All economic decisions of fundamental nature were made in the Centre. The Periphery did not have any independence in decision-making. The Centre did not want the Periphery to have independent economic development.

To begin with, a strategy of import substitution along with devaluation to boost export earning was adopted and implemented by a number of Latin American countries, but, instead of promoting their independent economic development, this strategy landed them in greater difficulties. Hence a number of economists came out with the assertion that, unless these countries broke away from the world capitalist system, no development was possible.

There are three approaches to the problem of underdevelopment among Latin American countries. While all of them agree on the explanation of the basic roots of backwardness of Latin American countries, there is difference of opinion as regards the possibility of development within the framework of world capitalist system.

The Centre-Periphery thesis has good explanatory value for the historical roots of backwardness of the countries of the Third World. It does not gloss over the role of imperialism and colonialism. It also focusses attention of the tie up between the local elites and the elites in developed capitalist countries.

The thesis suffers from a number of weaknesses. It ignores the existence and the role of different classes in a backward countries. It lumps all the capitalists of a backward country together and declares them to be subservient to developed capitalist countries. In addition, it assumes that there is no rivalry and conflict of interest among developed capitalist countries and this is far from the reality.

17.9 KEY WORDS

Bourgeoisie: A class of capitalists, who in all developed countries, are now almost exclusively in the possession of all the means of consumption and of raw materials and the instruments of their production. This class of bourgeoisie is the economically dominant class and stands in oppositions to, and in conflict with the working class.

Dependence: A situation where backward countries have to rely on developed countries for promotion of their own economic growth. It also means that developing countries follow developed countries in the spheres of economy, education, culture and politics.

Devaluation: A reduction in the official exchange rate between a country's currency and those of the rest of the world. It is done basically to increase export earnings because exports become cheaper and the volume of demand for them increase and to reduce the import bill as imports become dearer.

Dualism: The coexistence at one place of two situations which are mutually exclusive. To give an example, the coexistence of a segment of population which is highly educated along with vast masses who are illiterate.

ECLA (Economic Commission for Latin America): A regional organisation of the United Nations system located in Santiago (Chile), devoted to the study of the economic trends and problems of Latin America.

Import Substitution: A deliberate attempt to promote the domestic industries, producing goods which are till now imported. It requires adoption of steps that can discourage the purchase of imported goods and make people buy domestic substitutes. A country going in for import substitution imposes protective tariffs and physical quotas on imports.

Latin America: It includes South America, Central America, Cuba, Puerto Rico, the Dominican Republic and some small islands where Spanish and Portugese are spoken.

Monopoly Capitalism: A stage of capitalism characterised by monopolies, playing a predominant role. In other words, we can define it as a stage of capitalism in which competition among industrial capitals being replaced by monopolies. This was particularly witnessed at the end of nineteenth century.

Multinational Corporation (MNC): An international or transnational corporation with headquarters in one country but branches located in a number of countries.

Periphery and Centre: The world is divided into two categories. The first consists of developed capitalist countries and they constitute the Centre; the rest of the countries belong to the Periphery and they have no role of vital nature of influencing the course of world capitalist development.

Spread Effects: Impact of an action felt beyond the place where it takes. For example, a steel mill is set up at a place but its impact in terms of influence on economy, culture, urbanisation and so on is felt on adjoining towns and villages.

Terms of Trade: The ratio of a country's average export price to its average import price. If the ratio increases, terms of trade are supposed to be improving or becoming favourable. If it declines, terms of trade are supposed to worsen.

Underdevelopment: An economic situation where there are persistent low levels of living, widespread absolute poverty, low availability of social services, high birth and death rates and so on.

17.10 SOME USEFUL BOOKS

Baran, Paul A., 1982. *The Political Economy of Growth*, People's Publishing House, New Delhi (For 17.2).

Bernstein, Henry (edited), 1976, *Underdevelopment and Development : The Third World Today, Selected Readings*, Penguin Books, New Delhi. pp. 13-80 (For 17.2, 17.3, 17.3.1 and 17.3.2).

Bottomore, Tom et. al. (edited), 1983, *A Dictionary of Marxist Thought*. Basil Black-well, London, pp. 115-117, 224, and 312-317 (For 17.2 and 17.7).

Cockcroft, James D. Andre Gunder Frank and Dale L. Johnson, 1972. *Dependence and Underdevelopment: Latin America's Political Economy*, Anchor Books, New York (For 17.2, 17.3.1 and 17.6).

Frank, Andre Gunder, 1984. *Critique and Anti-critique: Essays on Dependence and Reformism*, Macmillan, London (For 17.2 and 17.3.1, 17.5 and 17.6).

Kruijer, Gerald J., 1987, *Development Through Liberation: Third World Problems and Solutions*, Macmillan Education Ltd., Hampshire.

Seers, Dudley (edited), 1981, *Dependency Theory: A Critical Reassessment*, Francis Pinter (Publishers) Ltd., London.

Todaro, Michael P., 1981. *Economic Development in the Third World*, Longman, New York, pp. 62-85.

Munoz, Heraldo, 1981, *From Dependency to Development: Strategies to Overcome Underdevelopment and Inequality*, Westview Press, Boulder, Colorado, pp. 15-41.

17.11 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) (a) F (b) F (c) F (d) T
- 2) Read Sections 17.1 and 17.2 and answer the question.
- 3) Read Section 17.2 and answer the question.

Check Your Progress 2

- 1) Read Sub-section 17.3.1 and answer the question.
- 2) Read Sub-section 17.3.1 and answer the question.
- 3) Read Sub-section 17.3.3 and answer the question.

Check Your Progress 3

UNIT 18 GROWTH IN DUAL/LABOUR SURPLUS ECONOMY

Structure

- 18.0 Objectives
- 18.1 Introduction
- 18.2 Characteristics of a Dual Economy
- 18.3 Sociological Dualism : Boeke
 - 18.3.1 Characteristics of Dual Economies
 - 18.3.2 Policy Suggestions
 - 18.3.3 A Critique : Technological Dualism
- 18.4 The Lewis Model
 - 18.4.1 The Framework
 - 18.4.2 The Dynamics
 - 18.4.3 An Assessment
- 18.5 Strategy of Development : Rosenstein-Rodan
 - 18.5.1 The Options before Less Developed Countries
 - 18.5.2 The Task Ahead
 - 18.5.3 The Big Push
- 18.6 Let Us Sum Up
- 18.7 Key Words
- 18.8 Some Useful Books
- 18.9 Answers/Hints to Check Your Progress Exercises

18.0 OBJECTIVES

This unit discusses a particular aspect of developing countries — that of dualism and consequent surplus in labour. After going through this unit you should be in a position to identify:

- the conditions that give rise to a dual economy,
- the way in which a dual economy is a labour surplus economy, and
- the process of absorption of the indigenous economy into an expanding economy.

18.1 INTRODUCTION

In the previous unit we have given a brief sketch of the concept, 'dualism'. However, the emphasis there was on the presence of the rich and poor countries alongside at the international sphere and the process of development in less developed countries through financial and technological aid from developed countries creating a situation of perpetual dependence. You may recall from EEC-01 the growth models of Harrod-Domar, Solow and Kaldor. These are aggregative models and consider the whole economy a homogeneous mass. In practice, however, the situation is quite different in developing countries. Here, there are pockets of affluence amidst vast areas of poverty. Hence, the aggregative models become no more relevant in such circumstances. The problem in developing countries is the coexistence of altogether two different sectors with different production, organisation and distribution set up.

economy can be divided into two main sectors: (1) an advanced sector largely associated with organised industrial sector, and (2) a backward sector which is unorganised, agricultural and rural.

The term 'dualism' was originally coined by Boeke in 1953 in the context of his socio-economic studies of Indonesia. However, the pioneering work on the dual economy models started with Authur Lewis in 1954. Later on significant contributions are made by Nurkse, Jorgenson, Ranis-Fei, Higgins, Harris and Todaro and many others. In this unit we will limit ourselves to the discussions on Boeke, Lewis and Rosenstein-Radan.

18.2 CHARACTERISTICS OF A DUAL ECONOMY

From the analysis of the very characteristics of such a dual economy to be discussed below in details, it will be self-evident that the overall progress of such an economy must necessarily deal with the problems of both growth economics and development economics simultaneously.

One of the main characteristics of a dual economy by which it is so termed is that two different socio-economic-technological environments co-exist within the same country. The two environments are generally called as 'advanced' sector and 'backward' sector.

As to the social and economic distinction, the backward sector is largely peasant-owned. Its mode of production is pre-capitalistic in the sense that it uses relatively little wage-labour or rented-land. The producers retain most of the product for self-consumption. The functional distribution of income among the various inputs to the production process and the demarcation between subsistence and surplus are all blurred in such a sector. Here per capita income is very low, (open) unemployment and (disguised) under-employment are its persistent features. All these make this sector economically stagnant.

The advanced sector, on the other hand, has a capitalistic mode of production in the sense that here wage-labour mostly works with capital (i.e., plant and equipment) whether privately or socially owned. Most of the product produced is sold in the market with some consideration for profit or surplus. Functional distribution of income between labour and capital as well as the division between surplus and subsistence is here satisfactorily defined in terms of the distinction between profits and wages. Here degree of industrialisation is high, factors of growth are in operation, productivity and wages increase and per capita income is very high.

As to the technological distinction, the two sectors have different methods of production. Depending on the natural resource endowment of the economy, such discrepancy can act as a constraint. This can limit output in the backward sector but not in the advanced sector. For instance, land may be one important and scarce factor in the backward sector while it is far less important in the advanced sector. Both sectors, of course, use capital of different forms. These factors of production, however, are not easily transferable or shiftable from one sector to the other. The backward sector is mostly traditional using backward, primitive methods of production. Also it has high labour-to-capital and labour-to-land ratio along with very low labour productivity. Advanced sector, on the other hand, is modern using advanced, mechanised methods of production with very high labour productivity. Subsistence economies may be characterised by three related features: (i) lack of specialisation on a significant scale, (ii) lack of regular production of a surplus with a view to sale, (iii) stationary technology.

Existence of dualism is a history-old phenomenon. Dualism developed historically through the opening-up process of backward regions by the industrially advanced countries through trade and/or colonisation. According to this historical-descriptive

agricultural sector, to the advanced industrial sector. As a result of such transformation, dual economies have mostly undergone a process of unbalanced growth, in the course of which a relevant part of the system has lagged far behind the other.

The main characteristics of a dual economy, thus, can be summarised as the following four points:

- 1) The advanced and backward sectors co-exist and there is much difference in the mode of production and organisation of these two sectors.
- 2) The coexistence is not transitional or short-term but chronic in nature.
- 3) The gap between both the sectors has a tendency to widen rather than diminishing.
- 4) The existence of the advanced sector does little or nothing to pull up the lagging sector.

Check Your Progress 1

- 1) Describe the characteristics of traditional sector.

.....

.....

.....

.....

.....

.....

- 2) Describe the characteristics of modern sector.

.....

.....

.....

.....

.....

.....

- 3) What are the main elements of dualism?

.....

.....

.....

.....

.....

.....

.....

.....

.....

18.3 SOCIOLOGICAL DUALISM : BOEKE

J.H. Boeke's dualistic theory is of special interest and importance because, on the one hand, his analysis was based on Indonesian experience and, on the other hand, it led him to highly pessimistic views on policy.

Social dualism, according to Boeke, is the clashing of an imported social system with an indigenous social system. Most frequently the imported social system is capitalism

But it may be socialism or communism also. This simultaneous development of one culture along with another is out of trade or colonialism.

18.3.1 Characteristics of Dual Economies

'Dualistic' for Boeke, is virtually synonymous with Eastern. Dualism arises from a clash between East and West. Boeke had the belief that the East and the West would never meet. In Eastern society there is **limited needs** in sharp contrast with the unlimited needs of a Western society. An important feature of an Eastern society in Boeke's views, is the almost complete absence of profit seeking behaviour of the producers. There is no professional trading and no industrial enterprise with a positive attitude towards investing capital and of taking the risk of investment. Lack of business qualities, lack of elasticity of supply, lack of organisation, discipline and corrective local specialisation are the important features of an Eastern industry. Another characteristic of these eastern societies is the importance attached to social needs. Possessions in the form of cattle, land, clothes and the fulfilment of social duties is not because of their economic usefulness nor the individual service they render. It is a matter of secondary importance whether the land produces reasonable profit in proportion to the money paid for it, whether the cattle can be made reasonably useful to their owner in his own business, whether the clothes cover, protects, warms the wearer or affects him pleasantly in any way. The determining factor is the social system and what the society think of the possessor.

Whereas agriculture is the dominant source of income and considered as a way of life, the role of industry is supplementary. This makes the industries very little remunerative, the technique of production being obsolete, traditional and averse to capital investment. All these are in sharp contrast to industries of Westernised, capitalistic sector.

Because of these differences between the Eastern and the Western economies, Boeke believes that Western economic theory is totally inapplicable to underdeveloped areas. Western economic theory is based on unlimited wants, a money-economy, and corporate industrial organisation. Moreover, Western theory is designed to explain capitalist society, whereas the Eastern society is pre-capitalistic in nature. So, the allocation of resources and the distribution of income cannot be explained in terms of the marginal productivity theory, mainly because of the immobility of resources in an Eastern society.

18.3.2 Policy Suggestions

This picture of social dualism in underdeveloped areas leads Boeke to pessimistic views on policy formulations. Boeke concludes that the process of social disintegration in dual societies cannot be reversed because it is not possible to transform the operating forces into the opposite of what they are. So the existence of dualism is to be accepted as a long-run phenomenon, and this acceptance leads to two conclusions: (i) one policy for the whole country is not expedient and (ii) what is beneficial for one section of the society may be harmful for the other.

Efforts to introduce scientific farming and mechanisation in agriculture will be a failure because the mental attitude of the farmers cannot be changed in the process. The culture of the village community is perfectly adapted to the environment. The existing agricultural system, whatever may be its degree of backwardness, is a result of adaptation. So the methods of Eastern agriculture cannot be improved.

As for industry also, Boeke believes that technological progress along Western lines is impossible. Eastern producers will not adapt themselves to the Western technology. Indeed, if Eastern enterprises endeavour to initiate Western methods, they merely lose their competitive qualities.

Similarly Boeke believed that the government cannot do anything about the unemployment problem of underdeveloped areas. Because, dealing with them would lead to a financial burden which is far beyond the means of the government.

Economic development of any kind is hampered by limited wants. An increase in

and fall in prices. So Boeke had little to suggest by way of positive policy, as a substitute for the technical and capital-assistance approach. However, his idea seems to be that any industrialisation or agricultural improvement must be a slow process, small scale and adapted to dualistic framework. What this policy means in concrete terms is not spelled out.

18.3.3 A Critique: Technological Dualism

Boeke explained the problem of dualistic development in terms of sociological explanations. However, to many, dualism can be readily explained in technological and economic terms.

Several authors, particularly Benjamin Higgins, have suggested the existence of technological dualism in developing countries. According to this view, the production function used in the traditional sector is far different from that in the modern sector. In this interpretation dualism is associated with structural unemployment or technological unemployment. This implies a situation where productive employment opportunities are limited, not because of lack of effective demand but because of resource and technological constraints in the two sectors.

The traditional sector, generally, is engaged in peasant agriculture, handicrafts and other very small industries. The products of such activities can be produced with a wide range of production techniques. The capital and labour can be combined in a number of ways to produce these goods, i.e., the capital output ratio is variable. With abundance of labour the production process in this sector is labour intensive.

In the modern sector, on the other hand, there is limited degree of substitutability between labour and capital. The capital-output ratio in this sector is fixed. Production process in this sector is capital intensive. The activities in this sector comprise plantations, mines, oil fields and large scale industries.

In this dualistic economies the development of modern sector was largely due to the inflow of foreign capital. Because of modern technology and efficient management this sector expanded. However, the population growth rate was much higher than the rate of capital accumulation. As a result the modern sector was not capable of absorbing the existing and additional labour force.

As the traditional sector has a variable factor combination in the production process the surplus labour force had to enter into the traditional sector. As labour supply increased in the backward sector, in the initial phase it resulted in bringing more land under cultivation. Eventually, land being a scarce resource, the excessive labour-intensive method of cultivation decreased the marginal productivity of labour to zero or even negative. This is the stage of **disguised unemployment**.

The abundance of labour in the traditional sector provided no incentive towards relatively higher capital intensive production process and thereby to increase labour productivity. On the other hand, in the modern sector, technical progress was in favour of more capital-intensive technique thereby reducing employment opportunities further in this sector.

Check Your Progress 2.

- 1) Boeke emphasise the social factors to describe dual economies. Substantiate.

.....

.....

.....

.....

.....

.....

.....

.....

2) What are the policy suggestions, if any, according to Boeke?

.....
.....
.....
.....
.....
.....
.....
.....
.....

3) What is technological dualism?

.....
.....
.....
.....
.....
.....
.....
.....
.....

18.4 THE LEWIS MODEL

In contrast to Boeke, Lewis gives an optimistic, and at times considered ambitious, model for the development of underdeveloped countries.

You should note at the outset that what is conventionally known as the Lewis model occupies a very small portion of Lewis' (1954) long essay "Economic Development with Unlimited Supplies of Labour". It is essential to read the essay in its entirety if you wish to appreciate Lewis' sweep and breadth of ideas. Lewis' work occupies a seminal place in the literature despite its many analytical loose ends.

18.4.1 The Framework

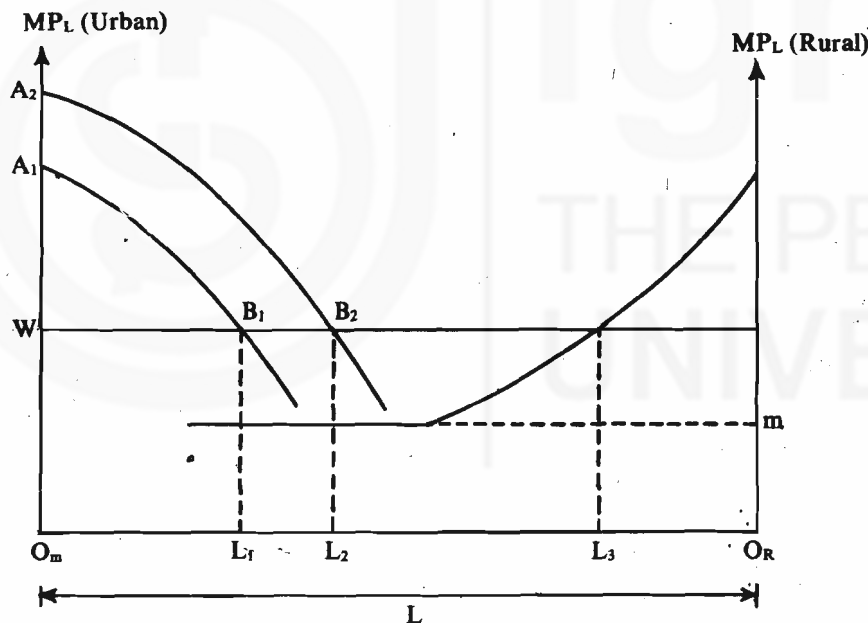
The Lewis model is a long-run analysis of the development process of a dual economy. It traces the path, over time, of a poor economy getting gradually industrialised. Lewis has made the following five assumptions in his model:

- 1) The economy is divided into two sectors – a backward, predominantly rural sector and an advanced industrial sector where the market operates.
- 2) The advanced sector utilises capital and labour. The important factors of production in the rural sector are labour and land.
- 3) The labour supply is perfectly elastic in the rural sector. This implies (a) the real wage rate in the rural sector is constant usually at the subsistence level, and (b) the marginal productivity of labour in the rural sector is zero. The latter can be interpreted as, if some workers are withdrawn from the field the output will not decline. Such a situation is termed disguised unemployment.
- 4) The productivity in the advanced sector is much higher than that in the rural sector.
- 5) In the advanced sector labour is paid a wage rate equal to marginal productivity. However, in the rural sector, wages are not related to marginal productivity (otherwise the zero marginal productivity would mean zero wage).

Lewis describes his model as a 'classical' one, in the sense that there is an unlimited labour supply at the subsistence wage in the rural sector. More precisely, this means that at the subsistence wage there is an excess supply of labour and this excess supply is sufficiently large so that the employer, when considering employment expansion, does not face the problem of rise in wage rate or a rationing or quota being imposed in the labour market.

If the capitalist sector wishes to draw on this unlimited supply of labour, it cannot, however, do so at the subsistence wage. It has to pay a higher wage, which is a mark-up on the rural subsistence wage, let us say, m . This, according to Lewis, could be 'because of psychological cost of transferring from the easy going way of life of the subsistence sector to the more regimented or urbanised environment' or 'it may be a recognition of the fact that even the unskilled worker is of more use to the capitalist sector after he has been there for some time than the raw recruit from the country'. While these explanations are not to be dismissed, they are clearly not completely convincing. For the time being, we treat the rural-urban wage gap as exogenously given.

To understand Lewis model let us consider Fig. 18.1. Let L be the total amount of labour in the economy (ignoring the important issue of increasing population). Let the rural marginal product curve of labour be horizontal over a considerable stretch with the marginal product being more or less around subsistence level. This is shown in Figure 18.1. Here O_R is the origin for the rural sector and O_M is the origin for the



modern sector. The wage in the urban sector, W , is considerably higher compared to the subsistence level, m . We assume that it is rigid downwards, i.e., it cannot fall below subsistence level because of exogenous reasons. Assume, for the moment, that both sectors produce the same good. In the initial period the marginal product curve of labour in the urban sector is A_1B_1 . The urban employer is a wage-taker, that is, he cannot influence the wage rate rather he accepts the on-going market wage rate. Clearly, in order to maximise profit he employs OL_1 units of labour. The remaining labour $L - O_M L_1 = O_R L_1$ remain in the rural sector and receive the wage rate, m .

18.4.2 The Dynamics

This may be referred to as a snapshot view of the Lewis economy. This has also been, in many ways, the starting point for much of the literature on dual economy analysis. As far as Lewis' view is concerned, the central theme is the dynamics of the system.

It is assumed that workers do not save because they are too poor. Surprisingly, rural landlords also do not save because they spend their rental income on luxurious consumption. Thus, the backward sector does not save. Only the modern sector capitalists save, and for simplicity, it is assumed that they save their entire profit.

augmented by the profit in period 1. This profit in period 1 (or increased capital stock in period 2) is equal to A_1B_1W in Figure 18.1 (assuming for simplicity that depreciation is zero). Because you may note that the total product in the industrial sector is $A_1B_1L_1O_M$ (area under the marginal product curve). Out of this, the share of the labour is $O_ML_1B_1W$ (wage rate multiplied by units of labour employed) and the profit is A_1B_1W (the residual). For details on this break up refer to Block 7 of EEC-01. In accordance with standard theory it is assumed that the marginal product of labour rises as the capital stock increases. Hence, the marginal product curve of labour in period 2 lies above A_1B_1 . Let this upward shifted marginal product curve in period 2 be A_2B_2 . Consequently, employment in the industrial sector rises to O_ML_2 and rural employment is O_RL_2 . The profit in the urban sector is given by A_2B_2W . As before, this is invested and a further upward shift in the urban marginal product curve of labour takes place. This relentless cycle of surplus, reinvestment and growth continues. Hence, steadily the industrial sector absorbs the surplus labour force of the rural sector.

The process continues with the wage rate in industrial sector remaining constant up to the point O_ML_3 . At that point the character of the economy changes in an important way. From here onwards the wages in the two sectors begin to move upwards and they maintain parity. Also at this point the gap between rural marginal product and the urban wage disappears. This is considered to be the stage where commercialisation of agriculture begins. This is the famous 'turning point' and from here onwards the economy begins to look very much like a developed economy. The classical assumption of unlimited labour ceases to hold. What is known as the Lewis model ends at this point.

18.4.3 An Assessment

The Lewis model generated a lot of interest among development economists. In the sixties there were many attempts to restate it more formally (among the more interesting being Ranis and Fei, 1961, and Jorgenson, 1967). The main concern of this literature is to examine the turning point in the long run process described by Lewis.

The Lewis model has been subjected to criticism from various perspectives.

Lewis assumes that the capitalists maximise profits. But while the objective of profit-maximisation is well defined in a static context, it can be quite ambiguous in a dynamic model such as this. On reflection, it becomes clear, that by this assumption what Lewis means is that in each time period the capitalist maximises profit. It follows consequently that in each period the capitalist chooses his labour input in such a way that the marginal product of labour is equal to the wage rate. Clearly this assumption cannot tell us how much the industrialist invests because that is an intertemporal decision ranging over a number of periods. So Lewis' assumption that capitalists invest their entire profits is a separate and distinct assumption.

Hence, instead of assuming a single objective function for the capitalist and deriving various behavioural postulates, Lewis begins by assuming two behavioural rules. This, in itself, is not objectionable, but it is important to check the implication of such behaviour.

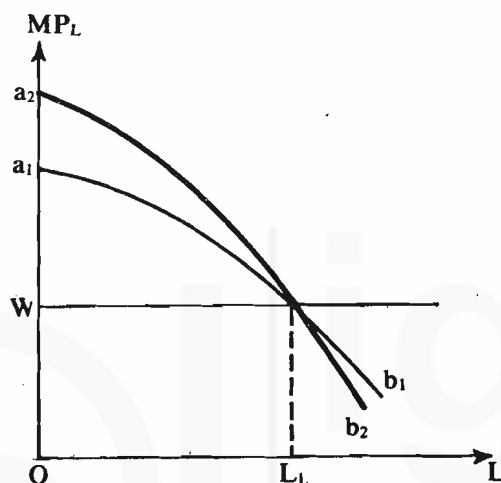
The trouble arises when we relax the assumption of a single good. Let us assume, as does Lewis, that the industrial sector and the agricultural sector produce two different goods. With this, the question of terms of trade between agriculture and industry comes into play. This places serious obstacles in the path of development described above.

Suppose there are many producers in the industrial sector and they are all price-takers (the argument is strengthened if we assume a monopoly). Let the price of the industrial good in terms of the agricultural good be P . A representative producer's output, X , is a function of capital, K , and labour, L . Within each period, K is fixed. Given that W is expressed in terms of agricultural goods, the amount of

This is depicted in Figure 18.2. The curve a_1b_1 shows the value of marginal product curve (i.e. $PX(L, K)$) as a function of L . L_1 is the equilibrium employment.

In reality, the determination of P is subject to a complex general equilibrium analysis. For simplicity, it is reasonable to assume that P falls as the total industrial output increases relatively to the rural one.

If in period 1, each firm invests its profit, $a_1b_1W_1$ (Fig. 18.2) then the marginal physical product curve will shift upward. But the value of marginal product curve need not shift similarly (for example, it may shift to a_2b_2), because with the higher industrial output, the price P will be lower. In fact, it is quite possible that the value of marginal product curve (at the new equilibrium price) will lie to the left of a_1b_1 .



This highlights two important difficulties. First there arises a question of capitalists' rationality. If investment in the first period diminished profits in the second period, would it not be more reasonable for the capitalists to invest less in period 1 and earn more profits in period 2? Lewis is not unaware of this difficulty, and he discusses it, somewhat tangentially in terms of some ideas of Malthus, Ricardo and Marx. While his discussion is interesting, he dismisses this criticism for reasons which are not too convincing. There is, however, a good argument which neutralises the above criticism. If the urban sector is composed of a sufficiently large number of capitalists then the fact that the total urban investment causes a deterioration in the terms of trade in the next period would not enter into any individual capitalist's calculations. Thus investment would not be held back for this reason.

While this is true this criticism nevertheless draws our attention to the question of investment criterion. Surely a capitalist would consider the rate of return to his investment. If it is too low, he will definitely not put the entire surplus as investment. It is, therefore, important to recognise that the proportion of profit, that is ploughed into investment, is a variable controlled by the capitalist and is liable to change depending on the rate of profit and other signals in the economy. And it is possible that an adverse movement in these signals may lead to a halt in the development process because of the capitalist's refusal to invest adequately.

In order to focus on the second difficulty let us assume away the above problem by supposing that capitalists mechanically invest all their profits. But as we have already seen, this will adversely affect the terms of trade; and this may be so adverse that the value of marginal product curve for labour shifts downward.

This implies the interesting possibility that even if capitalists behave exactly as postulated by Lewis and invest all their profits, urban employment may fail to grow. So, beginning from a primitive dual economy the forces which Lewis wrote about may not be present and may not move the economy in the direction suggested. On the other hand, the process itself generates forces which leads to stagnancy well before such a happy state emerges.

4) What is Harris-Todaro model on?

.....
.....
.....
.....
.....

18.5 STRATEGY OF DEVELOPMENT: ROSENSTEIN-RODAN

It is generally agreed that industrialisation of 'international depressed areas like Eastern and South-Eastern Europe (or the Far East) is in the general interest not only of the less developed countries, but of the world as a whole. It conforms to the view that poverty anywhere is a threat to humanity everywhere. The aim is achieving a more equal distribution of income between different areas of the world by raising incomes in depressed areas at a higher rate than in the rich areas.

18.5.1 The Options before Less Developed Countries

There are two fundamentally different ways of industrialisation of those areas:

- i) Eastern and South-Eastern Europe should industrialise on its own, aiming at self-sufficiency, without international investment. That would require 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. This way of industrialisation presents grave disadvantages:
 - a) It can only proceed slowly, because capital must be supplied internally curtailing the standard of living which is already at a very low level;
 - 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 and the reduction in the output of the world as a whole; and
 - c) The difference in world economic structure is most clearly seen in the development of heavy industries. Building up heavy industries in these backward areas at a great sacrifice of consumption 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.
- ii) The second way of industrialisation based on specialisation and transfer of resources would integrate these economically backward countries into the world economy which would preserve the advantages of an international division of labour. This would, therefore, result in the increase in output of the world as a whole. It would be based on substantial international investment or capital lending. This way presents several advantages.
 - a) It could proceed more quickly and at a relatively smaller sacrifice of present consumption in less developed countries.
 - b) The labour-intensive, i.e., light industries would develop in overpopulated areas. This would, to a large extent, solve the unemployment problem.
 - c) Even for the purpose of an expanding world economy, the existing heavy industries in the already developed countries could certainly supply all the needs of the international depressed areas.

18.5.2 The Task Ahead

An institutional framework different from the present one is clearly necessary for the

- a) International investment in the nineteenth century was largely self-liquidating, that is, returns to the investment would be sufficient to repay the debt, based on exchange of agrarian and industrial products. Now-a-days liquidation can no longer be assumed to be 'automatic', although the problem can be solved if it is properly planned.
- b) Existing institutions of international investment (floating of shares and loans) are inappropriate to the task of industrialisation of such vast areas. Such investments deal with too small units and do not take advantage of external economies. Capital goes mostly to individual enterprises. There has never been a scheme of planned industrialisation comprising a simultaneous planning of several complementary industries.
- c) Technological progress was the main driving-force of development in the nineteenth century. Industrialisation in international depressed areas, on the other hand, requires the application of existing technical knowledge.
- d) The increase in overhead costs and fixed capital since the nineteenth century has raised the risk of loss of capital. This has lowered the mobility of resources and the flexibility of the economic system. The average size of the firm is now substantially larger than that in the nineteenth century.
- e) Political risks of international investment are higher today than in the nineteenth century. State supervision and guarantees can substantially lower risks. However, active participation of the State in economic life is a new factor which must be taken into account.

Clearly this way of industrialisation is preferable to the autarkic one. It is a tremendous task, almost without historical precedent. There is no analogy to the process of industrialisation in the early nineteenth century for a number of reasons which may be mentioned briefly before being examined in more detail. In what follows arguments are submitted tending to show why the whole range of industries to be created are to be treated and planned like one huge firm or trust.

18.5.3 The Big Pus

The first task of industrialisation is to provide for training and 'skilling' of labour which is to transform the peasants of backward areas into full-time or part-time industrial workers. The automatism of laissez-faire would not succeed in doing this. It is not profitable for a private entrepreneur to invest in training labour. There are no bondages on workers – an entrepreneur who invests in training workers may lose capital if these workers leave that firm after training. 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 industries to be created when taken as a whole. However, it may represent irrecoverable costs for a smaller unit.

This is not, however, the most important reason in favour of such a large investment unit.

Complementarity of different industries provides the most important set of arguments in favour of a large-scale planned industrialisation. In order to illustrate the issue involved, let us adopt a somewhat roundabout method of analysing two examples. Let us assume that 20,000 unemployed workers in backward economy are taken from the agricultural sector and put into a large shoe factory. They receive wages substantially higher than their previous agricultural wage. It would be impossible to put them into industry at their previous wage rate. They need more foodstuffs than they had in their agrarian semi-unemployed existence. Also foodstuffs have to be transported to towns and the workers have to pay for housing accommodation. If these workers spent all their wages on shoes, a market for the products of their enterprise would arise representing an expansion which does not disturb the pre-existing market, and a bigger part of the problem would be solved.

The trouble is that the workers will not spend all their wages on shoes. If, instead, let us assume one million unemployed workers are taken from the agricultural sector

supply-demand imbalance can be avoided in such a situation. It would create its own additional market, thus realising an expansion of world output with the minimum disturbance to 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 excess supply in some sectors and excess demand in other sectors. It is in this sense that it is a special case of 'external economies'.

It may be added that in the highly developed rich countries with more variegated needs it is difficult to assess the prospective demand of the population. Rosenstein-Rodan claims, in case of underdeveloped countries, it is not as difficult to foresee on what the formerly unemployed workers would spend their wages.

Check Your Progress 4

- 1) What are the policy options before less developed countries according to Rosenstein-Rodan?

.....
.....
.....
.....
.....
.....
.....
.....

- 2) What are the policy suggestions for less developed countries?

.....
.....
.....
.....
.....
.....

18.6 LET US SUM UP

Dual economy refers to the existence of asymmetries in production and organisation in a developing economy. This asymmetry turns out to be a significant factor in dual economy models. A number of models have appeared describing different forms of asymmetries and rigidities in developing countries.

A common feature of all dual economy models is the co-existence of two different sectors. They are termed by so many names: modern and traditional, advanced and backward, rural and urban, agricultural and industrial, capitalistic and pre-capitalistic. Very often these terms are used interchangeably.

In this unit we discussed the social dualism model of J.H. Boeke. According to him the constraints before the dualistic economies are mainly sociological factors. As these factors cannot be changed in the short run he gives a pessimistic opinion about the future development prospects of dual economies. Technological dualism, although explains the characteristics of dual economies in terms of economic and technological factors it offers little towards policy suggestions. Lewis gives an optimistic and dynamic model of development of dual economies. His views on absorption of surplus labour is considered a pioneering work. Rosenstein-Rodan

18.7 KEY WORDS

Dual economy: The characteristics, largely that of less developed countries, where two distinct sectors with different levels of development in production technology, organisation and distribution coexist. One sector is advanced, modern while the other is backward and traditional.

Unbalanced growth: As opposed to balanced growth where all the important sectors of an economy grow simultaneously, in unbalanced growth there is uneven growth for the important sectors of the economy.

Functional distribution of income: Distribution of income amongst the important factors of production, i.e., rent, profit, wage and interest. For an economy one can study the characteristics of income distribution amongst households (called personal distribution) or amongst factors of production (called functional distribution of income).

Economic development and Economic Growth: At times these two terms are used interchangeably. However, there is one basic difference between them. Economic growth refers to the increase in GNP or in per capita income. On the other hand, economic development means much more than mere growth. When a country experiences economic development there are structural changes like rising share of industry in GNP (and declining share of agriculture), increase in urbanisation, changes in consumption pattern as people can afford consumer durables and leisure time apart from fulfilling basic needs and mass participation in the production process. Economic growth and economic development both involve rise in per capita income but development implies more than such a rise. One can have growth without development but one cannot have development without growth.

18.8 SOME USEFUL BOOKS

Ghatak, Subrata and Ken Ingersent, 1984, *Agriculture and Economic Development*, Select Book Service Syndicate, New Delhi.

Meier, G.M. (ed.), 1976, *Leading Issues in Economic Development*, Third Edition. Oxford University Press, New York.

Higgins, Benjamin, 1990, *Economic Development*, Universal Book Stall, New Delhi.

Todaro, M.P., 1982, *Economics for a Developing World*, Longman, London.

18.9 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) Your answer should include the methods of production, management and organisation of the traditional sector. See Section 18.2.
- 2) See Section 18.2 and answer.
- 3) Your answer should include the four main characteristics of dual economies.

Check Your Progress 2

- 1) Bring out the important elements in the characteristics of dual societies. The important ones are limited needs, social values and lack of enterprise. See Sub-section 18.3.1.
- 2) Boeke paints a gloomy future of dual economies. He has little to suggest. The best way for developing eastern societies is to leave it to themselves. See Sub-section 18.3.2.

Check Your Progress 3

- 1) See Sub-section 18.4.1 and answer.
- 2) See Sub-section 18.4.2 and answer.
- 3) See Sub-section 18.4.3 and answer.
- 4) See Sub-section 18.4.3, particularly the last paragraph.

Check Your Progress 4

- 1) See Sub-section 18.5.1 and answer.
- 2) See Sub-section 18.5.2 and answer.



UNIT 19 UNEQUAL EXCHANGE, GLOBAL ACCUMULATION AND UNDERDEVELOPMENT

Structure

- 19.0 Objectives
- 19.1 Introduction
- 19.2 Capitalist Accumulation and Unequal Exchange: The Genesis of Underdevelopment
- 19.3 Capital-Labour Relations: The Unequal Exchange
 - 19.3.1 Surplus Value
 - 19.3.2 Exploitation of Labour
- 19.4 Global Accumulation
 - 19.4.1 Exploitation of the Colonies
 - 19.4.2 Trade in Forced and Indentured Labour
 - 19.4.3 Mechanism of Slave Trade
- 19.5 Extraction of Surplus: Indian Case
- 19.6 Long-term Impact of Colonialism on International Division of Labour
 - 19.6.1 Deindustrialisation of Colonies
 - 19.6.2 Commercialisation of Agriculture
- 19.7 Manifestation of Unequal Exchange: Behaviour of Terms of Trade
- 19.8 Deteriorating Terms of Trade in More Contemporary Times
- 19.9 Let Us Sum Up
- 19.10 Key Words
- 19.11 Some Useful Books
- 19.12 Answers/ Hints to Check Your Progress Exercises

19.0 OBJECTIVES

After going through this unit you should be in a position to:

- identify the process of capitalist accumulation;
- explain the mechanism of surplus extraction from the colonies to the metropolis; and
- identify the impact of international division of labour on terms of trade.

19.1 INTRODUCTION

Different countries have registered uneven growth giving rise to the dichotomy of developed and underdeveloped countries. The two sets of countries show striking contrasts in their relative economic strengths. In one, there exists a situation of plenty while in the other, people are deprived of the means even for bare survival. This gap between the rich and the poor has been widening constantly: in 1976 the richest country in the world had a per capita income 41 times that of the poorest, and by 1990 the richest had a per capita income 56 times that of the poorest.

Underdevelopment is, thus, not a historical accident—it is the creation of the process through which the global economy has evolved in the past few centuries. How the

underdeveloped regions of the world have emerged and how they are caught in the vicious circle of perpetuating underdevelopment is what we shall try to explore here. We would try to situate underdevelopment in a historical context and would bring out the factors which have caused the problem to appear in the form as we see.

19.2 CAPITALIST ACCUMULATION AND UNEQUAL EXCHANGE: THE GENESIS OF UNDERDEVELOPMENT

Underdevelopment has been visualised as the inevitable consequence of capitalism. The unique character of capitalism as a mode of production is its motive for increased accumulation of capital. In fact, the basis for the existence of capitalism lies in the fact that it is able to carry out expanded reproduction of capital. In other words, a capitalist is able to increase the value of the stock of capital at his command at the end of every production cycle. The process which is the driving force of capitalism can be understood better thus: capitalists enter into the market with certain amount of money—their capital stock—which they use to initiate the process of production. At the end of the production process and the sale of the output, they realise an amount which is more than the initial amount of capital with which they had started the production process. Without this capacity to expand the stock of capital, capitalists and hence capitalism would not survive. But how do the capitalists manage to bring about this increase in the stock of money capital and thereby ensure not only the survival but also the prosperity of the system?

Capitalists maintain and strengthen their economic power in the system by extracting surplus from labour and marketing it as surplus value. This is the most simple presentation of the dynamics of capitalism as was underlined by Karl Marx and which has formed the basic framework on which all later literature on the subject have been based. The capital-labour relation is critical for an understanding of unequal exchange because in the ultimate analysis, the logic of capitalism is dependent on this relationship. An unequal exchange thus generated in turn creates conditions for capital accumulation to take place.

19.3 CAPITAL-LABOUR RELATIONS: THE UNEQUAL EXCHANGE

In the process of production under capitalism, two classes of individuals are involved. The capitalists own the factories and the equipment, or what Marx called the means of production. The labourers or the workers do not own any means of production, and they offer to the capitalists their own skill; or simply the labour power. A capitalist buys labour power by paying the labourers, or the workers as wages an amount which corresponds to the worker's means of subsistence. Marx explains how the value of labour, or his wages and his means of subsistence are determined: "the value of labour power is the value of the means of subsistence necessary for the maintenance of the labourers... His means of subsistence must be sufficient to maintain him in his normal status as a labouring individual." The means of subsistence for which workers are paid wages are thus the very minimum that is required by the workers for their survival.

A capitalist buys labour power and the raw materials to start his production process. At the end of this process he has a mass of produce which he sells in the market. Between the buying of the raw material and labour power from the market and selling the output, the capitalist manages to increase the amount of money that he originally began with when he started the production process. How does this happen?

19.3.1 Surplus Value

Marx indicated that the contribution to the increased capital stock of the capitalist comes from the workers he employs. This happens as labour adds more value to the

raw materials and machinery by producing the output than what he is paid as wages. Note that what the workers are paid as wages is equal to the means of subsistence. If the value of the means of subsistence is assessed, it may be found to be equivalent to the output a worker is able to produce in, say, four hours. And the workers are asked to work much longer, say, eight hours a day. This implies that after the production has proceeded for four hours the worker has added value to the material and machinery used up, a value that is sufficient to cover means of subsistence. In other words, he has worked enough to earn his wages. If the process of production were discontinued at this stage the capitalist would be able to sell the product for just enough to reimburse himself for his outlays made at the start of production. But the worker has sold himself to the capitalist for an entire working day, of say eight hours, and he earns his wages by working for the eight-hour day. Thus, the capitalist, by paying the worker an equivalent of only half a day's output, is able to pocket the other half for himself, which is the surplus he realises from the sale of his product.

19.3.2 Exploitation of Labour

The process of surplus generation for the capitalists, thus, involves exploitation of labour, paying labour less than what he contributes to the process of production. The greater is the exploitation of labour the more is the generation of surplus and more effective is the process of accumulation. Thus, the process of enrichment of the owners of capital and the impoverishment of labour lies behind the accumulation of capital. These concepts and process are explained in Block-9 of EEC-01.

Check Your Progress I

1) Explain the concept of surplus value.

.....
.....
.....
.....

2) What is meant by exploitation of labour?

.....
.....
.....
.....
.....

19.4 GLOBAL ACCUMULATION

From our discussion here it would be easy to see what situation is likely to emerge at the global level as a result of the dynamics of capitalism. The owners of capital have been the developed countries, the capitalist nations, who have been able to garner capital over centuries, and these countries have carried out exploitation of labour in the rest of the world to increase accumulation of capital. The surplus extracted by the capitalists in the colonies was often not invested in the country where it originated, it was used in the process of building up the capital base in their home countries (the metropolis). And, herein lies the main part of the explanation of underdevelopment. We would discuss some of the major forms by describing the process through which exploitation was carried out.

History tells us that there have been several mechanisms through which unequal exchange has existed in international trade. Colonialism provides the best known early evidence of a system where unequal exchange was practiced in the most blatant manner. The underdeveloped countries of today were colonised by the capitalist nations, and the colonies became an easy source for the latter to extract surplus which aided the process of capitalist accumulation.

Since the fifteenth century, when the sea-routes to America were discovered by the Europeans, the newly discovered land and their people were subjected to exploitation which lasted for centuries. The American aborigines became the first to be caught in the vortex of colonialism which spread later, in the seventeenth and the eighteenth centuries to the other continents—Asia and Africa.

19.4.1 Exploitation of the Colonies

The Portuguese and the Spanish were the first to emerge as colonial powers in the world. In the early sixteenth century, the Spanish overthrew the Aztec empire in Mexico and the Inca empire in Peru. The "conquistadors" (as the colonial power was called) captured the political power with the sole aim of exploiting the Amerindian (American Indian, the original inhabitants of America) labour and to make fortunes as quickly as possible.

But excessive exploitation of the Amerindian labour, combined with the outbreak of epidemic, led to a severe depletion of the local population. The exploitation took several forms,

- a) the Amerindians were confined to special villages and their labour was controlled by the the Spanish officials and settlers;
- b) the local population was often uprooted from their territory and were sent off to work in distant mines,
- c) the Amerindians were deprived of their best pieces of land and of essential sources of water supply, which the colonial settlers appropriated, resulting in a sharp decline in their incomes. On the land the Amerindians could manage to retain possession, they were forced to grow crops they were not familiar with,
- d) the Spanish introduced livestock-farming in densely populated areas. The Amerindians often practiced shifting cultivation so that their areas of circulation were never clearly demarcated. The livestock farming of the Spanish encroached upon the land of the local people and over a period of time the cattle population was able to evict the humans.

The initial rounds of colonial exploitation, thus, led to a systematic dispossession of local people of their traditional means of livelihood, and which eventually resulted in substantial reduction of the Amerindian population. In 1519, the Amerindian population in New Spain (Mexico and parts of Central America) was between 20 and 28 million and in less than a century, in 1605, they numbered only about 1 million.

19.4.2 Trade in Forced and Indentured Labour

Decline in population in the colonies made it imperative for the colonial powers to look for other sources of labour. Africa became the source of supply of slaves to the colonies. Slave trade was never an unknown phenomenon in the past. The Arabs had traded in African slaves for centuries. But the magnitude of slave trade from the seventeenth century carried out by the European colonial powers was unprecedented.

The demand for slaves came not only from the early colonial powers, Spain and Portugal, but also from other European nationals when they took over control of other territories and started large scale plantations of commercial crops. The trade in slaves increased several fold in the late seventeenth century as the market for sugar and other tropical products grew rapidly in Europe. The conditions of work were extremely inhuman and this caused great number of slaves to die. Fresh supplies were therefore needed continually to replenish to stock of the dying slaves. The situation became such that the expanding capitalist enterprise in the colonies in the Western Hemisphere was devouring entire communities in Africa, having already destroyed the local Amerindians in the sixteenth century.

This enterprise which was very profitable for the plantation owners and the European countries, was disastrous for the local population. The life of an average human being in Jamaica, a British colony, was valued at slightly more than twice the value placed

on a typical unit of livestock on the plantations. The situation in the Spanish colonies was probably much worse as plantation there was less capital intensive than that in the British colonies. Hence, the conditions of exploitation were more crude in Spanish colonies compared to others.

Trade in slaves was carried out by the four maritime powers, viz., Portugal, Holland, France and Britain. These nations supplied slaves to their own colonies as well. This enterprise of supplying slaves which started as a joint enterprise of the European nations, eventually became a virtual British monopoly as the country gained naval supremacy over others. The profits from the slave trade were theirs for the taking.

19.4.3 Mechanism of Slave Trade

An entire network of trade developed around slave trade, particularly after the Industrial Revolution took roots in Britain. The slaves and the slave-based plantations became the life-line of the industries, providing the inputs in the form of commodities and capital.

The mechanism functioned as follows: the slave traders obtained the slaves from the African Chiefs by paying them goods manufactured by the growing industry in Britain. The slave traders sold the slaves to the planters. These planters produced commodities like sugar in plantations. These produce were in turn sold to Britain and the northern colonies (later to become the USA).

The northern colonies provided the planters with foodstuffs, timber, etc. and obtained manufactured products from Britain. The West Indian colonies generally had a trade surplus with Britain and the northern colonies had a deficit which was partly covered by capital exports by Britain. The colonies thus got into this situation of running a trade surplus vis-a-vis the metropolitan centre but against this trade surplus the former could make no gains. The trade surplus was balanced by the colonial powers by charging the colonies a "price" for governance as was the case of "Home Rule Charges" imposed on India. Export surplus did not provide the necessary finance for making investments since all exports earnings were siphoned off by the colonial masters. The pattern of trade discussed here quite clearly brought largesse to the colonial powers which helped them in their attempts to increase their control over larger parts of the world. Extraction of surplus from the colonies was the sole objective and this was achieved through the unequal relations in trade that grew up.

Colonialism brought in its wake appropriation by the colonial powers of all forms of capital from the colonies. Human capital, in the form of slaves, was a very important source of capital that was drained out. This form of exploitation involving human capital took place not only in the regions which had a history of slave trade, like Africa but also in regions which had no known evidence of having slave trade. India was among the more prominent of these countries which suffered this form of exploitation.

Significantly, forced and indentured labour were taken out of India and taken to the West Indies, Natal, Fiji, Malaya, Mauritius and Ceylon at a time when slave trade and slavery were abolished. In 1807, slave trade was officially abolished in 1833 slavery in British colonies was to have ended.

In India, colonial exploitation and unequal exchange took place in a different form. The form of exploitation that was adopted in case of India was of a different character than what was witnessed in the colonies that we discussed above. We discuss it now.

Check Your Progress 2

- 1) What are the different forms of exploitation that took place in northern colonies?

.....
.....?
.....

- 2) How did the mechanism of slave trade take place?

19.5 EXTRACTION OF SURPLUS: INDIAN CASE

British domination over India began with the conquest of Bengal in 1757 by the East India Company. Since then and upto 1813, the East India Company had a monopoly of trade between Europe and the East. Together with the control over the Indian economy which they were gradually establishing, the company was able to extract substantial surplus from the captured land. The company extracted surplus in the form of a tribute.

The exploitation of India during 1757 to 1813 was carried out with the East India Company as the legal monopolist in trade. It was able to perform this function with the active assistance of a number of private European traders whose cooperation was very important in trade with China, the country with which Britain had strong trading links. Part of the surplus realised by the company through trade and revenue collected from Bengal was utilised to extend British rule in the rest of the country and to balance trade with China (Britain had a trade deficit with China until the first quarter of the nineteenth century). The rest of the surplus was transferred to Britain as unrequited export surplus in goods or bullion.

Available estimates of "drain of wealth" or unrequited exports from Bengal or British dominions in India in general put the amount appropriated by Britain at Rupee 38 million for the period of 1757-80, Rupees 1.78 million annually for the period 1783/84 to 1792/93, and between Rs. 3 million and Rs. 4 million per annum between the years 1813 to 1822. From these estimates of drain it has been assessed that at least 5 to 6 per cent of the gross domestic product, not taking into account the non-material part of the domestic product, was being siphoned off by the company and which was forming a part of Britain's stock of investible capital for its own industries.

The importance of India in providing surplus to Britain grew by the middle of the nineteenth century. India not only generated a large surplus on her trade account, she also had a deficit with Britain in her balance of payments. India also maintained a large trade surplus with other parts of the world and with these regions Britain had a deficit in trade. The colonial Government used the trade surplus generated by India in its global trade to settle the deficits Britain was running with all these countries. Thus, the surplus from trade instead of coming to India was being routed out by the British colonial masters.

This pattern of trade and the consequent surplus extraction from India was to be a feature of British rule in India. India generated trade surplus consistently upto the end of the 1930s on its merchandise account as Table 19.1 shows.

Table 19.1
Export Surplus of British India on Merchandise Account
(1871/72 to 1938/39)

Period	Annual Average Value (Rs. 4000)
1871/72 to 1875/76	212,258
1876/77 to 1880/81	223,513
1881/82 to 1885/86	278,199
1886/87 to 1890/91	254,143
1890/91 to 1895/96	313,010
1896/97 to 1900/01	200,854

1901/02 to 1905/06	413,759
1906/07 to 1910/11	477,700
1911/12 to 1915/16	527,993
1916/17 to 1920/21	457,401
1921/22 to 1925/26	617,417
1926/27 to 1930/31	509,101
1931/32 to 1935/36	173,854
1936/37 to 1938/39	305,200

Source: Bagchi, Amiya Kumar, *The Political Economy of Underdevelopment*, Cambridge University Press, Cambridge, 1982, p.89.

This surplus, as indicated in Table 19.1, was appropriated by Britain by making India pay for the "cost of governance". Thus, not only was it setting its own trade imbalances with the rest of the world, Britain was siphoning off surplus generated by India in a more direct manner.

19.6 LONG-TERM IMPACT OF COLONIALISM ON INTERNATIONAL DIVISION OF LABOUR

Colonialism created the conditions leading to progressive underdevelopment of the colonies through direct exploitation that took the form of surplus extraction in several forms as we have discussed. Also, it developed a structure of international division of labour which allowed unequal ties between the colonies and the metropolis to perpetuate long after the colonies became independent. We would turn to this aspect of unequal exchange in the following discussion.

The long-term effects of colonisation can be seen in the emergence of an international division of labour of a definite character. Colonies were developed by the metropolitan centres as producers of industrial raw materials which could then be supplied to the industries that were fast emerging in the metropolis. Both agriculture and the mineral producing sectors were targeted by the colonial masters and most colonial economies functioned around these two sectors.

19.6.1 Deindustrialisation of Colonies

Industries in the colonies, in whatever form they existed, whether they were the small production centres of the artisans, or otherwise, went through a systematic course of destruction. The extent of deindustrialisation that the colonies witnessed comes very cogently through the experiences of a few colonies which are very well documented. India, one of the best documented cases, suffered deindustrialisation right through the nineteenth century and well into the twentieth.

The process of deindustrialisation of India began with the total destruction of its domestic cotton manufacturing capacity due to the steep increase in cheaper imports from the newly developing cotton mills in Britain. Upto the beginning of the twentieth century, India remained the major importer of cotton goods, often importing more than forty per cent of Britain's exports.

19.6.2 Commercialisation of Agriculture

Apart from destroying the existing indigenous enterprises and making India recipient of manufactured goods from Britain, the colonial rulers sought to change the character of domestic agriculture, in a manner which aided to the emergence of an international specialisation that the metropolitan centre was promoting. India, like all other colonies, was made to produce the raw materials which were then supplied to the newly emerging industries in Britain. As a result of this pressure, the character of agriculture in the colonies changed completely; subsistence agriculture was broken by introducing cash crops like cotton, indigo and jute needed by the industries.

Deindustrialisation suffered by the colonies helped strengthen the international specialization that the metropolis was attempting to introduce through colonial exploitation. The production system so introduced led to a clearly defined structure of international trade. Colonies were left to trade in commodities—the unprocessed raw

materials required by the industry—while the metropolitan centres, traded in the finished products of the industry. This pattern of trade created severe anomalies for the underdeveloped regions, a distortion that caused unequal exchange relations to develop and perpetuate right up to the contemporary times. How did this unequal exchange manifest itself? We come to this part now.

Check Your Progress 3

- 1) What was the medium of extraction of surplus from India to Britain?

- 2) International division of labour went against the interest of colonies. Justify.

19.7 MANIFESTATION OF UNEQUAL EXCHANGE: BEHAVIOUR OF TERMS OF TRADE

If the nature of exchange relations established through trade is to be assessed, terms of trade provides a very convenient way of assessment. In brief, terms of trade is a ratio of a country's export prices to import prices. This expression of terms of trade in its most commonly used variant, is called the net barter terms of trade. Two other expressions of terms of trade have also been suggested, (a) the gross barter terms of trade, taken as a ratio of the volume of exports and imports and (b) income terms of trade, which is also referred to as the "purchasing power of exports". The latter expression income terms of trade, indicates the level of imports in real terms that can be sustained by current export earnings.

Let us analyse the tendencies displayed by the terms of trade between the developed and the underdeveloped regions since the nineteenth century. We arrive at certain specific conclusions about the nature of exchange relations that have existed between these predominantly "industrial" and the "agricultural" countries. We had discussed earlier the process through which these "industrial" and "agricultural" countries had been created. Also, how deindustrialisation of the colonies made them predominantly agricultural countries.

Terms of trade between industry and agriculture (data for which are available from the third quarter of the nineteenth century) would explain the relative positions of the developed and the underdeveloped regions as they have participated in exchange relations.

Table 19.2
Relative Prices Behaviour of Raw Materials
and Manufactured Products (1876-1935)

Years	Ratio of Prices of Raw Materials to Prices of Manufactured Products in World Trade
1876-1880	147
1881-1885	145
1926-1930	118
1931-1935	93

Source: Amin, Samir, *Accumulation on a World Scale*, Monthly Review, New York, 1974, p.71.

Table 19.2 clearly indicates that the exporters of raw materials, the underdeveloped regions of the world, were continuously facing declining prices of their products vis-à-vis the manufactured products produced by the metropolitan centres. Thus, the underdeveloped regions, which were importing manufactured goods from the developed countries, were forced to pay increased price for these products. On the other hand, their own exports, i.e., the imports for the developed countries, were constantly becoming cheaper. This implied that while the earnings of underdeveloped countries from exports kept going down steadily, their expenditure on imports registered a continuous increase. A more complete picture of the unequal relations in trade between developed and developing countries can be seen from Table 19.3.

Table 19.3
Terms of Trade between Developed
and Underdeveloped Countries (1913-100)

Year	Export volume		Gross Barter terms of trade Developed / Under-Developed	Export Unit Values		
	Developed	Under-Developed		Developed	Under-Developed	Net Barter terms of trade Developed / Under-Developed
1876-1880	30	50	10	94	67	140
1896-1900	62	83	75	84	54	155
1913	100	100	100	100	100	100
1928	127	150	84	134	130	103
1937	107	175	61	118	100	118
1953	176	284	62	250	163	154
1962-63	315	450	70	255	143	177
1967-68	470	600	78	270	155	173

Source: Barratt Brown, Michael, *The Economics of Imperialism*, Penguin, London, 1974, p.249.

Table 19.3 tells us quite clearly that the price that underdeveloped country products were fetching in the world market was increasing much slowly as compared to the price of underdeveloped country exports. If the unit value of exports for both developed and underdeveloped countries is assumed to be Rs. 100 in 1913, in 1968, the price of developed country exports increased to Rs. 270, i.e. by 2.7 times, while the price of underdeveloped country exports remained only Rs. 155, an increase by only 1.5 times.

Table 19.3 shows another significant phenomenon viz., the volume of exports from underdeveloped countries have shown more improvement than those for the developed countries. Thus, while the underdeveloped countries were exporting larger volume of their products, in terms of earnings they gained much less as compared to the developed countries. The valuable resources of the underdeveloped countries were consequently getting sold at steadily decreasing prices.

19.8 DETERIORATING TERMS OF TRADE IN MORE CONTEMPORARY TIMES

The international division of labour that the metropolitan centres had thrust on the underdeveloped countries created structural rigidities in the latter to such an extent that they have not been able to get out of the exploitative clutches of the developed countries. Large part of the underdeveloped world still remains outside the modern system of industrialisation and they remain overwhelmingly producers of primary commodities. The poorest continent, Africa, still depends on export of commodities for earning most of its foreign exchange. 90 per cent of the export earnings of the African countries, even at the end of the 1980s, come from commodity trade. The least-developed countries, as a whole, depend on export of commodities to the extent of 85 per cent of their earnings. And for these commodities, the price level has declined most sharply, particularly in the decade of the eighties. Commodity prices in the period 1980-89, decreased at an average annual rate of 6.7 per cent. This sharp fall in prices implies that to maintain their level of export earnings, the poorest nations are compelled to export increasingly larger volumes of the commodities.

Not only that the most poor nations face this crisis of deteriorating terms of trade, all the underdeveloped countries also face similar conditions. Terms of trade decline was experienced by all these countries irrespective of whether the countries were producing primary commodities or manufactured goods, they had to carry the historical legacy of unequal exchange. The terms of trade had declined to such an extent that the underdeveloped countries as a whole lost US \$ 1238 billion in export earnings. This implies that if their price of exports had not declined as it did, these poor countries would have been able to earn this amount. What is loss for the underdeveloped countries is gain for the developed countries, and thus the historical phenomena of accumulation by perpetuating underdevelopment lingers on.

Check Your Progress 4

- 1) Define the following terms
 - a) Net Barter Terms of Trade
.....
.....
.....
 - b) Gross Barter Terms of Trade
.....
.....
.....
 - c) Income Terms of Trade
.....
.....
.....
- 2) Show that the terms of trade of underdeveloped countries is deteriorating.
.....
.....
.....
.....

19.9 LET US SUM UP

Underdevelopment is a creation of the historical process through which capitalism has developed over the centuries. Capitalism has developed and prospered through its ability to accumulate capital. The capitalist has the capacity to multiply the amount he invests at the beginning of the production process. This expanded reproduction of capital is possible through the exploitation of the workers he employs, who are paid as wages an amount which is less than the contribution they make in the production process. The exploitative characteristic of capitalism was carried out at the global level through colonial exploitation by the capitalist nations.

Colonies became an easy source for the capitalists to find capital required for accumulation. In some of the early colonies, exploitation of labour in the most virulent form became the source of surplus extraction. Later, in colonies like India, the process of surplus extraction took a different form. The colony was put through a system of trade in which the surplus it generated by trading with the rest of the world was appropriated by Britain to settle the latter's deficit with other countries. The colony was also obliged to pay for the cost of governance by Britain, which helped the colonial power to accumulate further.

The colonies were converted into producers of raw materials for the growing industries in the developed regions, a role they have played even after they have ceased to be colonies. This caused long-term problems for the erstwhile colonies as the

prices of raw materials were declining constantly in the world markets and their earnings from exports were declining. While the underdeveloped countries have lost their export earnings, this loss to the poorer nations became the source for accumulation by the developed regions.

19.10 KEY WORDS

Accumulation of Capital: Capital accumulation has been viewed in two distinct ways by economists. The most common has been the expansion of the productive potential of an economy with a given technology, through 'ploughing back' part of the surplus arising out of production. This view, therefore, refers to the availability of surplus and the motivation to reinvest it. The second view has been the transformation of the technical and productive organisation of the economy. This view is, also referred to as technical progress.

Means of Subsistence: The minimum level of goods and commodities required to maintain the production capacity of labour. A reduction in wages below the subsistence level was assumed to hamper the efficiency of labour. A high wage may encourage population growth and eventually bring down the wage rate to subsistence level.

Surplus Value: In the class societies, the continuation of the ruling class requires that it be able to extract a surplus product from the subordinate classes. This means that every ruling class must somehow get the subordinate classes to work beyond the time necessary to produce their own means of consumption. It is this surplus labour time which creates the requisite surplus product. According to Marx in Capitalist Societies the Capitalists own the capital while labour supplies its labour power. The value added in a product from raw materials and machineries is by the labour force alone. The subsistence wage received by labour is worth much less in value than the work done by labour. In the process there is exploitation of labour.

19.11 SOME USEFUL BOOKS

Amin, Samir, 1974, *Accumulation on a World Scale*, Monthly Review Press, New York.

Emmanuel, Arghiri, 1972, *Unequal Exchange*, Monthly Review Press, New York.

Bagchi, Amiya Kumar, 1982, *The Political Economy of Under-development*, Cambridge University Press, Cambridge.

Baran, Paul A, 1973, *The Political Economy of Growth*, Penguin, London.

Barratt Brown, Michael, 1974, *The Economics of Imperialism*, Penguin, London.

Furtado, Celso, 1973, 'Elements of a Theory of Under-development — the Under-developed Structures', in H. Bernstein (ed.), *Underdevelopment and Development*, Penguin, London.

Frank, Gunder, 1975, *On Capitalist Underdevelopment*, Oxford, London.

Magdoff, Harry, *The Age of Imperialism*, Monthly Review Press, New York.

Magdoff, Harry, 1978, *Imperialism: From the Colonial Age to the Present*, Monthly Review Press, New York.

Sweezy, Paul, 1964, *The Theory of Capitalist Development*, Monthly Review Press.

Viner, Jacob, 1937, *Studies in the Theory of International Trade*, Harper and Brothers Publishers, New York.

Williams, Eric, 1944, *Capitalism and Slavery*, Russel and Russel, New York.

19.12 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) See Sub-Section 19.3.1 and answer.
- 2) See Sub-Section 19.3.2 and answer.

Check Your Progress 2

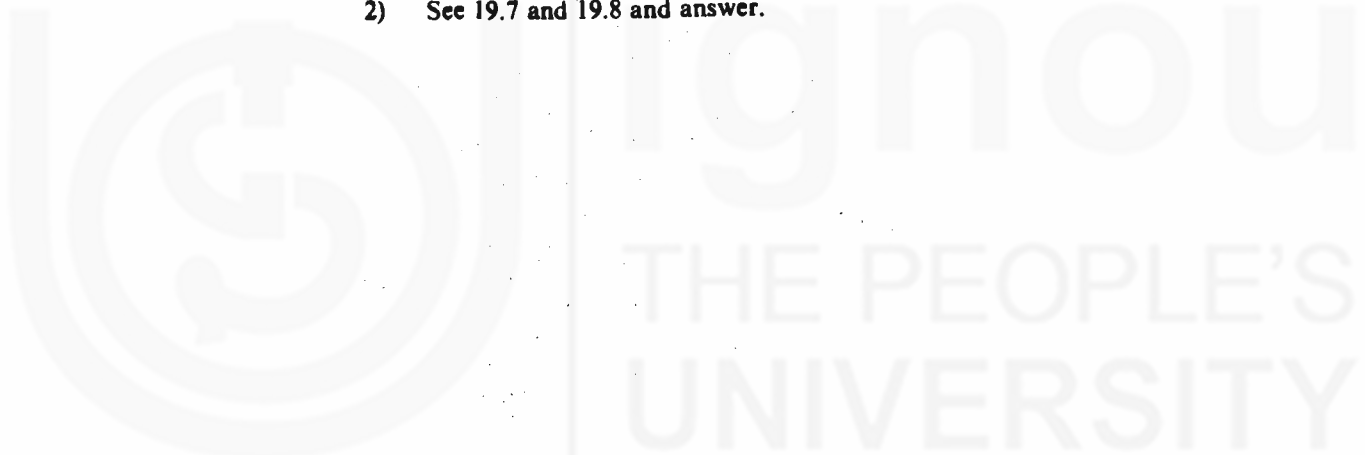
- 1) See 19.4.1. Discuss the problem of exploitation of Amerindians.
- 2) See 19.4.3 and answer.

Check Your Progress 3

- 1) See 19.5 and answer.
- 2) See 19.6 and answer.

Check Your Progress 4

- 1) See 19.7 and answer.
- 2) See 19.7 and 19.8 and answer.



UNIT 20 THE CRISIS IN DEVELOPMENT PLANNING: CONTEMPORARY ISSUES

Structure

- 20.0 Objectives
- 20.1 Introduction
- 20.2 What is Planning?
 - 20.2.1 Evolution of Development Planning
 - 20.2.2 How is the Economy to be Planned?
- 20.3 Removing Constraints on Investment
 - 20.3.1 Emphasizing Balanced Development
 - 20.3.2 The Element of Uncertainty
- 20.4 Mobilising Resources for Investment
 - 20.4.1 Mobilisation of Human Capital
 - 20.4.2 Generation of Marketed Surplus
 - 20.4.3 Linking External Sector to the Domestic Sector
 - 20.4.4 The Essentials of Planning: A Recapitulation
- 20.5 The East European Model of Central Planning
 - 20.5.1 Limitations of Centralised Planning System
 - 20.5.2 Reconsideration in the Planning Strategy: The Chinese Model
 - 20.5.3 Economic Planning in Japan
- 20.6 Planning Versus Market
- 20.7 Let Us Sum Up
- 20.8 Key Words
- 20.9 Some Useful Books
- 20.10 Answers/Hints to Check Your Progress Exercises

20.0 OBJECTIVES

After going through this unit you should be in a position to:

- explain the major facets of planning,
- explain the plan models followed by certain countries; and
- identify some contemporary issues concerning planning.

20.1 INTRODUCTION

The imperatives of economic development in most of the countries in the twentieth century have been sought by one fundamental question: should the process of development be planned by the Government or should it be left to the free operation of the market forces, without any intervention by the Government. This question arose prominently after the first socialist country, the Soviet Union, started the extensive exercise of planning its economic development in the late 1920s. Economic policies prior to the Soviet experience were led by the dictum of Adam Smith, one of the founding fathers of modern economics. According to Smith, any form of regulation of the economy by the Government was undesirable.

The emergence of the Soviet Union notwithstanding, free operation of the market came to be increasingly questioned by economists after the serious crisis in the 1920s

and 1930s. The great depression gave the indication that the free play of market forces did not necessarily bring about economic prosperity. It was suggested that resources must be employed in a planned manner to ensure economic development of nations.

The arguments for intervention in the market gathered strength from yet another set of studies which propounded the view of "market failure". This view discussed the inefficient allocation of resources that takes place under market mechanism. Although this view was formally put forth in the past few decades, the symptoms of what came to be termed as "market failure" were identified in an earlier period by A.C. Pigou. In 1932 Pigou had suggested that taxes and subsidies should be introduced to overcome the problems of inefficient allocation that the market brings with it. This, in effect amounted to recommending an interventionist system.

The "Plan versus Market" debate was thus introduced but the unquestioned superiority of one system over the other had not been conclusively established. For, if the argument in favour of planning and against the market mechanism found general acceptability in the early decades of the twentieth century, the recent decades have seen a diminished role for planning. This view against planning has taken shape following the crisis that the former socialist countries of Eastern Europe, which were centrally planned, went through. In response to the crisis, these countries gradually gave up their systems of planning in favour of the market mechanism. What has become quite clear from the historical experience of the former socialist countries is that the form in which they try to plan their economies is not efficient in any manner. But do these experiences only imply that the planning by its very nature is inefficient and that only the market mechanism is the alternative for ensuring development? This is the question we would address ourselves to here.

In trying to answer this, we would first discuss the essentials of development planning as have been indicated by the authors who brought the idea into prominence. We would then try to understand the form in which the former socialist countries had adopted the planning system and also indicate the limitations of the system. Finally, we would discuss the case of two countries—China and Japan, and the manner in which they have tried to adopt planning without getting into the systemic crisis as the Eastern European countries. The experience of these countries could provide important insights for us to understand what form planning should take in order to succeed.

20.2 WHAT IS PLANNING?

The essential of planning for economic development as indicated by Oscar Lange, one of the leading contributors to the debate on planning, consists in assuring an amount of productive investment which is sufficient to provide for a rise in per capita income. The strategic factor, according to Lange, is investment, or more precisely, productive investment. Having assured the availability of investible resources in adequate amount, the process of planning involves directing these resources into productive channels. This would ensure rapid growth of the productive capacity of the economy. The problems that development planning encounters are, therefore, two-fold: (a) mobilisation of resources for the purposes of productive investment, and (b) directing such investment in proper directions so as to realise faster growth of the economy.

These two fundamental issues on which development planning is supposed to be based are elaborated by several authors, including Oscar Lange himself. This has evolved a policy framework which could facilitate operationalisation of the principles laid out. Let us discuss this now.

20.2.1 Evolution of Development Planning

Development planning became a part of the policy framework adopted by most underdeveloped countries in the period immediately following the Second World War. The singularly important contribution towards the eventual acceptance of planning as a strategy was made by Paul Rosenstein-Rodan. Rosenstein-Rodan in a paper in 1943, put-forth what is known as the "balanced growth" doctrine. Rosenstein-Rodan was spelling out the prospects of industrialisation in South-Eastern

Europe and in that context he put forth the view that for an underdeveloped country to grow, it was essential to evolve a development plan which would ensure simultaneous and balanced growth of all sectors of the economy. The views of Rosenstein-Rodan are discussed in unit 18 of this course.

Rosenstein-Rodan's doctrine was elaborated further by his contemporaries like Maurice Dobb, Ragnar Nurkse and Arthur Lewis. These authors indicated the imperatives of adopting a framework in which development could be planned. The detailed discussion below would deal with this.

20.2.2 How is the Economy to be Planned?

Identifying the major constraints faced by the underdeveloped countries was the first step in the sequence drawn up by the authors. It was maintained that low level of initial investment was a major constraint. Nurkse, among others, provided an explanation for this phenomenon.

20.3 REMOVING CONSTRAINTS ON INVESTMENT

Nurkse pointed out that in underdeveloped countries it was the inducement to invest which was low. Further, low incentives to investment were set by the small size of the domestic market. Because of lack of expertise they could not capture foreign market also. The incentives to install capital equipment for the production of a certain commodity or service always depend to some extent, according to Nurkse, on the size of the market for the particular commodity or service in question. The crucial determining factor behind the market size in a country, in Nurkse's view, was productivity of labour or simply output per man-hour. Output per man-hour, in its turn, depended largely, though by no means entirely, on the degree to which capital is employed in production process. Higher the capital per labour, higher is the labour productivity. This, in other words, implies possibilities of expansion of the size of the domestic markets in the underdeveloped countries in the increased use of machinery and equipment.

20.3.1 Emphasizing Balanced Development

In suggesting increased use of capital Nurkse dwelt on the idea of balanced-growth or a synchronised use of capital in a wide range of industries. Most industries catering to mass consumption were thought to be complementary in the sense that they provided a market for and thus supported one another. Otherwise, if only a particular industry is developed, without enhancing production in others, there may be deficiency in demand for the product.

The balanced development of industries has advantages for the economy, a point emphasised by Nurkse himself and later by Maurice Dobb. Simultaneous development of industries created external economies, which took the form of influencing the development of one industry or sector by the growth possibilities of another. Dobb illustrates the process of creation of external economies as follows: The development of the transport sector or that of sources of fuel and power influence both the costs and market possibilities of diverse manufacturing industries. Similarly an engineering industry through its expansion can favourably influence the development of the industrial sector in general by providing the necessary inputs in the form of equipment and machinery. The external economies, Dobb explains, appears nothing less than the interdependence of different elements in an organic process of growth—an interdependence that strikes an essential balance without which growth may be impossible to achieve. Even if the growth process starts it may be quickly halted in the absence of complementarities.

20.3.2 The Element of Uncertainty

One important aspect of planning for simultaneous development of industries lies in the fact that planning process is able to circumvent critical limitations which an unregulated market, where individual firms take their decisions independently, faces. The most significant of such limitations is the element of uncertainty that confronts

an individual firm when it is taking investment decisions. The absence of perfect information normally characterises an unregulated market economy. Perfectly competitive markets, though considered ideal, and widely analysed in a theoretical framework, markets in reality are essentially imperfect in nature. An individual firm, for instance, does not have perfect information about the investment decisions being taken by other investors in the economy. Also, it is not certain of the future returns, demand for the product, taste of the people, etc. Uncertainty in such imperfect market would not allow the individual firm to take decisions as efficiently as would have been the case if perfect information was available. On the other hand, if all firms could be brought together through a planned effort then the individual firms intentions could be known and this would allow necessary adjustments in volume and timing of investment in the light of the knowledge obtained.

Uncertainty of the kind that the market introduces have been widely discussed in literature following the work done by Tjalling Koopmans. Koopmans referred to this uncertainty as "secondary uncertainty" which, according to him, was seen to arise from lack of communication, that is, from one decision maker having no way of finding out the concurrent decisions and plans made by others.

Elimination of "secondary uncertainty" was found to have attendant advantages: external economies could be generated as a result. This was pointed out by Tibor Scitovsky. In one of his extensive presentation on external economies, Scitovsky indicated that only if expansion in the industries were integrated and planned together only then the profitability of each of them would be a reliable index of its social desirability. Complete integration of all industries would be necessary to eliminate the divergence between private benefit and social benefit. Scitovsky's comment simply means that if all firms plan their production collectively there are possibilities of development and consequently benefits accruing to the public at large. In the absence of such collective action individual firms may not like to invest as they may be uncertain of future market trend and expected profits may not be adequate enough to justify the investment likely to be undertaken.

Check Your Progress 1

- 1) **How is the constraint of market size to be avoided?**
.....
.....
.....
.....
- 2) **What are the important issues those planning should solve?**
.....
.....
.....
.....
- 3) **How does the element of uncertainty influence investment?**
.....
.....
.....
.....

20.4 MOBILISATION OF RESOURCES FOR INVESTMENT

In addition to the limitations of the market constraint which discouraged investment in underdeveloped countries there is yet another problem to which several authors

have referred. This, like the first problem of improving the inducements to invest, could not be solved automatically by the market forces alone. This is the amount of investible resources available in these countries. Authors like Nurkse and Lewis emphasised two forms of resources. These are capital in the form of financial resources and human resources.

20.4.1 Mobilisation of Human Capital

Mobilisation of the mass of unemployed and underemployed labour was necessary for the purposes of capital formation in the underdeveloped economies. The view of W.A. Lewis on absorption of surplus labour are discussed in the previous block. Taking the surplus labour off land and setting them to work on capital projects like irrigation, drainage, roads, etc. was the mechanism suggested by Nurkse for mobilising the unutilised manpower in the underdeveloped countries. But this new work force would require wage-goods (food, clothing, etc.) and this was to be met by curbing consumption of the affluent classes. The contention of the authors arguing thus was that the affluent should be forced to save out of their high level of consumption and this saving could be used in a productive manner. Michael Kalecki, one of the main contributors in this debate, suggested a similar mechanism of curbing consumption and ensuring a smooth supply of wage goods enabling in the process the rate of saving to be kept high.

20.4.2 Generation of Marketed Surplus

It has been pointed out that resource mobilisation of underdeveloped countries was insufficient because the inadequacies in production system itself limited the volume of output. You may recall that the vicious circle of poverty operate in underdeveloped countries. Low level of investment results in low productivity. Low productivity gives rise to low per capita income. Low per capita income to low level of saving which in turn gives rise to low level of investment. This is particularly true of the agricultural sector, the largest sector in most underdeveloped countries, where the perpetuation of landlordism and other contracts arising out of semi-feudal relations in production affected the volume of production. The landlords carried out little improvements in the existing systems of production and as a result output growth in agriculture stagnated at a low level. The actual producers, the farmers, had no right over land they cultivated. Hence, they were reluctant to carry out any improvements in the methods of cultivation. The fear of eviction and uncertainty in weather multiplied this reluctance. Additionally, the farmers suffered exploitation in the hands of the intermediaries like the landlords and moneylenders by means of exorbitant rent and rate of interest. A large part of the produce was appropriated by these middlemen. The middlemen were thus diverting a large part of the surplus of agricultural sector and spending on unproductive channels like hoarding and luxurious consumption. This surplus could have been used in a more productive manner for the purpose of development.

Kalecki, through the analytical frame he developed, indicated that if the marketed surplus in agriculture (the wage goods sector) did not increase, an increase in the rate of investment in the economy as planned could not be realised. But the mere increase in the output of the farm sector is not enough to ensure that surplus is produced. It is also necessary to ensure that any increase in agricultural production is translated into marketed surplus immediately. But where the landlord and moneylender dominate the farm sector the automatic mobilisation of marketed surplus does not materialise. The element of control over the resources in the agricultural sector and the process of living off the surplus have restricted the flow of wage goods at the desired rate and thereby has retarded the rate of development.

If these constraints are not controlled it would perpetuate the phase of underdevelopment. It is therefore suggested that given the circumstances in the underdeveloped countries, efforts are needed to give a proper direction to the existing systems of production in the farm sector. Intervention to change this system has thus been regarded as one of the imperatives of planned development.

20.4.3 Linking External Sector to the Domestic Sector

Planned development of the domestic sector of the economy is not the only aspect of planning which the literature suggests—a similar planning is suggested in respect of the external sector as well. This is thought necessary because the excess consumption of the affluent classes in the economy has the potential of spilling over into the external sector. This could take place because with rise in income the rich would demand luxury consumption goods produced in the developed countries. If these goods are not produced in the underdeveloped countries, they would have to be imported. This excess consumption could then have its impact on the balance of payments, causing serious imbalances. Control over importables is therefore considered to be an essential part of planning in the underdeveloped countries.

Another important factor for planning external sector is the need of capital goods and technical knowhow. For increasing productivity and take advantage of the research and development taking place in developed countries, underdeveloped countries are dependent on the developed world.

Mobilisation of domestic and foreign resources for development have been often addressed to jointly through the so-called **two-gap models** of aid, trade and development. In these models, based on assumptions regarding a desired rate and pattern of growth, the anticipated gap between exports and imports on the one hand and the anticipated gap between savings and investment on the other have been estimated. Exports in most of the underdeveloped countries were found to be stagnant at a low level while imports experienced increase because development in these countries could not take place without resorting to imports. The anticipated trade gap, i.e., the gap between imports and exports, is often found to be larger than the anticipated investment-saving gap. To move out of this scenario the suggestion is made that there should be a plan to mobilise foreign resources in the form of aid and private capital transfers so as to ensure development without impediments.

20.4.4 The Essentials of Planning: A Recapitulation

The arguments advanced in support of planning as discussed above can be summed up as follow. Planning is considered as a preferred option because of three advantages it has over the market mechanism. These are, (a) it helps realisation of the requisite level of savings (domestic as well as foreign) for attaining the desired level of growth in the economy, (b) it helps in a balanced use of capital (previously accumulated and present investment) between sectors so that all the sectors become mutually supportive of one another in furthering the development process, and (c) it helps eliminating uncertainty to some extent by coordinating the operation of producers, raising possibilities of generating economies of scale in the process.

Planning is thus considered to have its advantages. But why did the planning systems in the former socialist countries meet with total failure? Our discussion now would deal with the planning systems evolved by the centrally-planned economies of Eastern Europe. We would indicate briefly the weaknesses of the centrally-planned system and then discuss the manner in which two countries—China and Japan—have adopted variations of a plan strategy which, unlike the East European model, have not been through a crisis.

Check Your Progress 2

1) What is the suggestion made by Nurkse for resource mobilisation?

.....
.....
.....
.....

2) What are the major problems deterring agricultural sector from generation of marketed surplus?

.....

20.5 THE EAST EUROPEAN MODEL OF CENTRAL PLANNING

The first formal planning framework for the Soviet Union was developed in the 1920s by G.A. Fel'dman. The framework developed by Fel'dman became the basis for the planning exercises in most of the centrally-planned economies of Eastern Europe, which like the Soviet Union had adopted the Socialist system.

The basic structure of the Fel'dman model is derived from the two sector model of Karl Marx. The model assumed a closed economy, an economy having no foreign trade. It assumes the existence of two sectors, one producing consumer goods and the other producing capital goods. The capital goods, as is assumed by Marx, consists of all such machinery, equipment and intermediate goods that are required for the consumer goods industries. The consumer goods are the final goods that go directly into the consumption basket.

In the model Fel'dman suggested, capital goods are assumed to be the only limiting factor of production that is, they are scarce. The size of the capital goods sector, therefore, holds the key to the size of the national economy. But once the level of output from the capital goods sector decided by the central planning authorities (for a specific increase in national income), the next step involves estimation of the appropriate level of inputs to sustain the level of output of the capital goods sector. For example, if a given volume of steel is decided to be produced the level of production of all the inputs directly and indirectly required for the production of the desired volume of steel output are to be obtained. This requires the production of the inputs in the steel making process, viz., coal, iron ore, limestone, in sufficient quantities. These levels are to be derived from the plan model, along with the machineries like blast furnaces and smelters and the infrastructural facilities like power, water and transport. For each sector, and further for each commodity to be produced in the economy, precise figures of inputs required and the output to be obtained are laid down by the central planning authorities by working out the material balances.

Production plans are worked out also for each enterprise in these centrally-planned economies. The planning authorities give each enterprise a production target which the latter is expected to fulfil within the time horizon adopted for the planning process. The management of the economy is thus conducted within this highly centralised structure.

The planning in East European countries was done within the framework of State ownership of property, that is, in the absence of private profit. Production, distribution and relative prices in the economy were fully controlled by the State. In other words, there was complete absence of a free market for commodities. Distribution, like production, was also carried out in the centrally-planned economies in line with the parameters set by the planning authorities.

Such voluminous exercise in planning was characteristic of all the centrally-planned economies.

20.5.1 Limitations of Centralised Planning Systems

The elaborate description of material balances characterised by Fel'dman planning model was, however, considered neither necessary nor sufficient for a good plan. Criticism against this sort of planning exercise has come from a protagonist of the planning system itself, Oscar Lange. Lange has commented on the mindless perfectionism in which some planners, especially in the centrally-planned economies, are engaged. According to Lange, active planning and effective control of economic development are possible without going into such details. Planning such details, in

Lange's view, inhibited effective management of the national economy. Too much details bore no relation with the actual process of planning, it rather emanated from the desire to move towards centralisation of day-to-day control over the economy.

Centralisation of economic authority through planning mechanism, as was seen in most socialist economies, created several problems. The character of management was highly centralised. The stress was more on investment and the general atmosphere of enterprises was one of scarcity. Within this environment the targets to achieve certain quantitative goals gave rise to a tendency at the enterprise level to hoard resources and invest too much. This view is expressed by a leading economist from a former socialist country, Janos Kornal.

The literature indicates a further distortion that the Soviet type planning could introduce in the economy. This is because of the over emphasis on industrialisation — particularly, the emphasis on heavy industry as opposed to the light, consumer goods producing, industries. At a sectoral level, this type of planning introduced another imbalance, the discrimination against agriculture. It was thought by the planners in these countries that the drive to increase the rate of industrialisation and maintaining stability in prices, there should be adequate supply of agricultural goods at fixed prices to the non-agricultural sector. But fixed prices of agricultural produce tended to offer lower returns to the producers in the farm sector. This issue was raised in the debate on Soviet industrialisation wherein it was generally maintained that the Soviet peasantry provided support to the growing industrial sector through the process of keeping prices constant. More recent studies have, however, questioned this widely held view.

The process of industrialisation through which centralised planning tends to discriminate against agriculture appears to have been tacitly admitted by another country that adopted Centralised Planning strategy, namely, China. China also had adopted the Soviet model but in course of time it made significant changes in its planning strategy. The discussion below would make clear the dimensions of change in planning that the Chinese have brought about. It is important to understand the Chinese model because they have re-framed their strategy to remove some of the distortions in the Soviet strategy referred to above.

20.5.2 Reconsideration in the Planning Strategy: The Chinese Model.

The main elements of change that the Chinese have adopted in their variant of planning are mainly on two counts. These are, (a) increasing the rate of growth of light industry by decreasing the ratio of accumulation (investment) in the national income, and (b) allowing the productive enterprises, both in industry and agriculture, to set their own production targets, instead of the planning authorities setting these targets as is done in the Soviet model. In the Chinese model the State is given the role of ensuring proportionate and coordinated growth of the national economy through overall balancing of sectors. Rather than adopting a centralised planning system, China has adopted a system that is close to indicative planning, a mechanism that has got identified with the French system of planning.

An important characteristic of the central planning model, namely, the absence of a market, was abandoned by China. In most sectors, except those catering to basic needs like fuel, grains and cloth, where the State authorities were involved in distribution, the direct producers were given freedom to market their products. As opposed to a complete centralisation of economic activities through planning, China adopted a system in which the market could be regulated in order to remove the distortions caused by the market. The State left a part of the production and distribution to the market which was to be a supplement to planned production and distribution. The market was playing a secondary and subordinate role to the state but it was considered essential.

Ownership of property was initially completely State controlled, but in recent years, there has been some shift away from complete State ownership.

China has, thus, attempted to arrive at a balance between complete regulation of all economic activities by central planning authorities and free operation of market forces. More akin to this Chinese model has been the Japanese system of economic

management which, as several authors have indicated, is planning in an operational sense of the term.

20.5.3 Economic Planning in Japan

The Japanese model, provided a framework for harnessing resources in a manner that could help develop the economy in the desired direction. The Japanese model was adopted later on by South Korea and Taiwan.

The uniqueness of the Japanese model of planning lay in the fact that it did not depend on public ownership of resources as is normally associated with planning, at least in the initial phases. Instead, it allowed private enterprise to grow, but within the framework evolved for the overall economic development.

Ten economic plans have been adopted so far by the Japanese in the Post-World-War period, beginning in the 1950s. The first economic plan, the Five Year Plan for Economic Self-Reliance was adopted in 1955. These plans have been the basis for Japan's economic success in the past few decades. The plans helped establish effective procedures to build an independent national economy through rapid industrial transformation.

The plan framework as adopted by the Japanese and spelt out in the 'National Income Doubling Plan (1961-1970)' was designed to provide a reliable overall perspective for development. The defects of the market mechanism were kept in view while developing the plan and its aim was to activate individual sectoral policies without centralised controls of forcible authority.

20.6 PLANNING VERSUS MARKET

As we see, planning strategy varies from country to country. Not only that, a particular country may change plan strategy over time keeping in view its needs and ideology. In the introduction to this unit we had mentioned about the debate over planning versus market. Although the superiority of one over the other is not clearly established, the recent trend has been in favour of the free play of the market. The controversy delve deep into political economy.

The classical economists suggested a laissez faire economy where the role of the government is kept to the minimum, viz. defence, administration and justice. They advocated that free play of the market forces would provide optimum allocation of resources in the economy. They even suggested free trade among nations on the basis of the theory of comparative advantage. The Say's law that "supply creates its own demand" was assumed to operate and maintain full employment in the economy. However, in the wake of unequal level of development among countries, and the fact that the entrepreneurs in less developed countries could not compete with their counterparts in the developed countries gave rise to the logic of 'infant industry' protection. The imposition of tariffs and quota restrictions hampered the free movement of goods and services among nations.

The 'Great Depression' (1929-32) falsified the classical economists' position that there could be macroequilibrium in the economy and no excess supply. The vast scale of unemployment and increase in inventories along with decline in aggregate output was noticed and classical suggestion could not cure the malady. J.M. Keynes, in such a situation, attributed emphasis on aggregate demand and advocated that deficiency in aggregate demand could lead to falling output and employment. To compensate the inadequate aggregate demand by general public, he suggested an increase in public investment. The Keynesian suggestion can be briefly put this way: If there is idle resources in the economy increase aggregate demand through increased public investment. On the other hand, if there is excessive aggregate demand giving rise to high rate of inflation reduce public investment.

Thus, there is a trade-off between unemployment and inflation. This you have read in EEC-01 in terms of Phillip's curve. However, such a trade-off between inflation and unemployment did not hold good during 1970s in the world economy. There was

widespread unemployment accompanied with high rate of inflation. Such a situation, termed 'stagflation meaning 'stagnation with inflation', made Keynesian suggestion ineffective.

The economics of Keynes and his followers, often termed 'Keynesian revolution', advocated wider role for government operation and intervention. The public sector entered into direct production of goods and services, not necessarily 'social goods'. The success of centralised economies inspired the developing countries for planning in a much bigger way.

However, 'monetarism' 'advocated mainly by Milton Friedman' undermined the role of government planning. Based mostly on empirical evidences the monetarists suggested that the government make the economy better by 'doing nothing'. They suggest free market operation and the government should control mainly money supply in the economy.

The 1970s saw the emergence of a new school of thought — the New Classical economics. Considered as a loose federation of 'monetarism' 'supply side economics' and 'rational expectations', the New Classicals are the advocates of free market. The rational expectationists believe that general public have their rational expectations mostly out of past experiences towards trends in the major macroeconomic variables like inflation, growth, interest rates, tax rates, etc. The general public take counter measures to neutralise the adverse impact of government policies. As a result government strategy become ineffective and real variables do not change. Only way to change real economic variable is by way of 'supply shocks' like manipulating the cost of production, rather than 'demand shocks' like influencing factors affecting aggregate demand. The New Classical economists advocate tax cuts, deregulation of the economy and reduction in public expenditure.

There is a tendency in the global economy towards free market undermining the role of planning. The dissolution of centralised planning in Eastern Europe and their movement to market economy has strengthened such a tendency. The operation of free market is at two levels: a) at the domestic level there is lesser role for government intervention and planning, and b) at the inter-national level there is emphasis on free trade.

Some diverse trends are taking place in the world scenario in recent years. There is controversy over the inclusion of the trade in services within the purview of GATT (General Agreement on Tariffs and Trade). Efforts are on to form an European Common Market with single currency by the European Economic Community. On the other hand there is the disintegration of the erstwhile USSR into independent market economies.

Check Your Progress 3

- 1) What are the basic elements of Centralised Planning?
.....
.....
.....
.....
- 2) Give a brief account of the debate on Planning versus market?
.....
.....
.....
.....

20.7 LET US SUM UP

In this unit, we discussed the essentials of planning. The constraints before developing countries, particularly inadequate mobilisation of resources, correcting regional imbalances and diluting the element of uncertainty. We also discussed the centralised plan models of East European countries and the planning procedures in China and Japan. Planning should provide indications of the directions of development. We also discussed the current trends in the debate over market intervention and planning.

20.8 KEY WORDS

Market failure: The important variables are left for the market to decide but no optimum allocation is achieved.

Resource Mobilisation: Transfer of resources to the government from rest of the economy which is not to be repaid.

Private benefit: The benefit accrued to the unit concerned.

Social benefit: The benefit to the economy as a whole.

Absorption of Surplus labour: The surplus labour in the rural sector is productively employed in the urban sector.

Wage goods: The essential commodities which are substantially consumed by wage-earners.

Marketed Surplus: The surplus from agricultural sector which is taken to the market.

Semi-feudalism: Feudalism is a stage of development, where production is mostly agricultural. A rigid class or status structure on the basis of land ownership is present. In the social pyramid, the lord who was granted an estate in return of military obligation to the monarch rented this land to 'serfs' in return for a rent and having his estate cultivated by these serfs. Proper market for labour and industrialisation process is yet to come in such societies.

Spillover: Certain goods cannot be consumed exclusively by the buyer. Rather the benefit of such goods accrue to others also. Such goods are termed social goods, and 'externalities' from such goods 'spillover' to others. A classic example could be the spraying of DDT in one's own house to kill mosquitoes. If others in the neighbourhood do not apply DDT simultaneously to eradicate mosquitoes completely, mosquitoes from the neighbourhood can come in next day itself. And if all others do apply, the person concerned need not spray as mosquitoes in the neighbourhood would be killed even if he does not.

Indicative Planning: The government does not issue instructions to the firms and financial institutions regarding their respective inputs and outputs as is the case in directive planning. The means employed to control current economic activities is broad macroeconomic policies. These policies indicate how the economy could develop; sometimes tax reductions are given to firms which move in the desired direction.

Tow-gap models: The economic models depicting the relationship between domestic saving-investment gap and balance of payments gap.

20.9 SOME USEFUL BOOKS

Bagchi, Amiya Kumar, 1987, *Development Planning*, In Eatwell, John. Murry Milgate and Peter Newman (eds.). *The New Palgrave: A Dictionary of Economics*, Macmillan, London.

Dobb, Maurice, 1960, *An Essay on Economic Growth and Planning*, Routledge & Kegan Paul, London.

- Kalecki, Michael, 1955, *The Problem of Financing Economic Development*, Indian Economic Review, February.
- Lange, Oscar, 1961, *Essays on Economic Planning*. Asia Publishing House, Calcutta.
- Lewis, W. Arthur, 1954, *Economic Development with Unlimited Supplies of Labour*, Manchester School of Economic & Social Studies, May.
- Muquio, Xue, 1981, *China's Socialist Economy*, Foreign Languages Press, Beijing.
- Nurkse, Ragnar, 1953, *Problems of Capital Formation in Underdeveloped Countries*, Basil Blackwell, Oxford.
- Rosenstein-Rodan, Paul, 1943, *Problems of industrialisation of Eastern and South-Eastern Europe*, Economic Journal, June-September.
- Scitovsky, Tibor, 1954, *Two Concepts of External Economies*, Journal of Political Economy.
- Tani, Kouichi, 1988, *Economic Planning and the Market Economy: Experience in Post-War Japan*, In Urrutia, Miguel and Setsuko Yukawa (eds.), *Development Planning in Mixed Economies*, The United Nations University, Tokyo.
- Phelps, Edmund S., 1985, *Political Economy: An Introductory Text*, W.W. Norton & Co. New York.

20.10 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

- 1) The concept of balanced growth suggest that demand for products of respective industries would be reinforced by one another thereby creating a market. See Section 20.3 and answer.
- 2) The central issues are resource mobilisation and investment in proper direction. See Section 20.2 and answer.
- 3) See Sub-Section 20.3.2 and answer.

Check Your Progress 2

- 1) See Sub-Section 20.4.1 and answer.
- 2) See Section 20.4 and answer.

Check Your Progress 3

- 1) See Section 20.5 and answer.
- 2) See Section 20.6 and answer.