ONE of the distinctive features of an under-developed economy is the prevalence of what our economists are in the habit of calling ‘disguised unemployment’. Too many people subsist on agriculture. Seemingly they are employed. But their employment is not wholly productive. It is not wholly productive in the sense that production does not suffer even if some of the so-called employed are withdrawn. The ratio of labour to land and other resources is so large that the marginal productivity of labour is reduced to zero, although the average productivity remains positive. And, unlike in the organised sector, it is thin average productivity and not the marginal productivity that determines the earnings, and hence consumption of the labourers. The result is that the marginal body of labourers consume, but they do not produce. They are employed physically, but not economically.

The organisational set-up (such as we have in a subsistence economy) is what makes for this. Farms consist of family holdings, and productive operations are done by the members of a family as a group. Labour is not, disassociated from capital, and workers may be said to be self-employed. There are the landlords and the money lenders. But they get their rent and interest at stipulated rates; they do not perform the function of an employer. Whatever output is derived from productive operations therefore vests in the family and is enjoyed by all the members irrespective of their specific contribution; the redundant members are not just thrown away. The share of output that goes to the redundant units of labour is of the nature of transfer income. If, of ten persons working in a farm, four are redundant, in the sense that the farm could be managed equally efficiently with six persons, then, from the economic point of view, 40 per cent of the output of the farm can be viewed as being transferred to unproductive consumers. It is as if the entire output is the contribution of six persons who just ‘save’ a part of this contribution and hand it over to the remaining four. Prof Nurkse calls this the ‘saving potential’ of a subsistence economy.

It is on this concept of saving potential as a concomitant of disguised unemployment that Prof C N Vakil and his colleague have built a theory of economic growth. Planning in an under-developed economy, if it is to be effective, must, according to our authors, take account of ‘disguised unemployment’ of the subsistence sector and make full use of the “saving potential” that is associated with it. The process can be initiated only if the increase in the volume of employment in the planned sector is made to exceed the addition to the labour force consequent on the growth of population. So long as our plan seeks just to absorb the additional labour force that comes into the market as a result of population growth, the disguised unemployment remains untouched and with it the saving potential. Once, however, our planned investment passes this limit, a cumulative process of expansion sets in. The argument in this context runs as follows:

Suppose that the value of wage-goods needed to employ an additional unit of labour in the planned sector is Rs 400 whereas the actual consumption of a corresponding unit in the subsistence sector is Rs 200. Then, if the planned sector can somehow secure an extra saving of Rs 400, the additional employment created will be two units instead of one. For, while with the ‘saving’ of its 400 done in the planned sector one unit of labour is productively employed, the withdrawal of this unit from the subsistence sector is accompanied by a release of Rs 200 worth of wage-goods. This can now be added to another equivalent bundle of wage-goods to be released if one more unit of labour is withdrawn from the subsistence sector. The economy is therefore in a position to absorb altogether two units of labour in productive employment, although the initial dose of saving was just enough for one unit. Saving thus breeds saving, and we have a so-called ‘multiplier’ effect on employment: the value of the ‘multiplier’ depending upon the ratio of ‘wage unit’ in the planned sector to what it is in the subsistence sector. The ‘saving potential’ that it carries is used as a supplement to whatever additional savings can be drawn from the rest of the economy. For this to happen, the rate of growth of employment must pass the critical limit, set by the growth of population. Our authors’ crusade against India’s Second Five Year Plan is based largely on this concept. The employment target set in the Plan is much too inadequate to draw in the ‘disguised unemployed and to bring the cumulative process into play.

However, if our authors had reflected upon their hypothesis a little more closely they would perhaps realise that they had started from the wrong end. Not that their proposition is wrong; of course it is not. So far as the arithmetic is concerned. But the way it is presented suggests a certain Lick of awareness of the obstacles to the growth of an under-developed economy. In their excitement at what they thought was a discovery they forgot to notice that if the proposition were put the other way, apparently forgetting that ‘labour’ and ‘wage goods’ are not additive. There are many such unpardonable lapses in the book against which the reader must guard himself.

† The term is used here to signify the actual consumption of a unit of labour.

** The authors use a term ‘employable unit’ in this context which they define as ‘labour plus wage' may be called the ‘consumption unit’ in the subsistence sector. The lower this ratio, the higher is the value of the ‘multiplier’.

So far, so good. The emphasis on the implications of ‘disguised unemployment’ for the economics of growth is commendable. The proposition that employment is limited by the flow of wage-goods that can be made available to labourers, though apparently commonplace, is worth emphasizing at a time when economic thinking is so widely influenced by the Keynesian theory of effective demand. In an under-developed economy, the scope for expansion of the current output of wage-goods is limited, and the Keynesian investment multiplier is insufficiently operative. Yet an opportunity for a ‘cumulative process’ offers itself in such an economy if the ‘disguised unemployment’ is released from the subsistence sector and the ‘saving potential’ that it carries is used as a supplement to whatever additional savings can be drawn from the rest of the economy. For this to happen, the rate of growth of employment must pass the critical limit, set by the growth of population. Our authors’ crusade against India’s Second Five Year Plan is based largely on this concept. The employment target set in the Plan is much too inadequate to draw in the ‘disguised unemployed and to bring the cumulative process into play.

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way round, it would take a form which has been familiar to most of us most of the time. Let us revert to our authors' example. The 'consumption unit', as we have called it, is Rs 200 and the 'wage unit' is Rs 400. Assume, with our authors, that along with the transfer of the 'disguised unemployed', the goods that they used to consume in the subsistence sector are also transferred to the planned sector. The market is then provided with an additional Rs 200 worth of wage-goods for each extra unit of labour employed in the planned sector. It is true, then, that if an extra saving of Rs 400 is made available in the planned sector, possibilities will be opened up for the employment of two units of labour instead of one which is the labour content of the extra savings, and the so-called multiplier effect will be operating. Now look at this same thing the other way round. A unit of labour is released from the subsistence sector and with it a bundle of goods worth Rs 200. The consumption unit thus released is not sufficient to provide employment to one additional unit of labour in the planned sector; the market has to somehow secure another Rs 200 worth of wage-goods by way of savings. The transfer of a unit of labour from the subsistence sector releases wage-goods whose value is only one-half of the actual wage that has to be paid if it is to be productively employed. If we look at the matter this way, which is the correct way, the 'consumption goods multiplier' takes on an altogether strange complexion and turns out to be a myth.

One feels tempted, at this stage, to turn back and to see wherein our crucial problems lie. The problem of growth in an under-developed economy with a large and redundant population is basically a problem of capital formation. Employment in the investment goods sector needed for capital formation is no doubt limited at any moment by the availability of wage-goods. But the output of consumption goods in general and of wage-goods in particular is itself a function of the stock of capital. An increase in the stock of capital increases the scope for the employment of labour, although during any given period of investment needed for the production of capital goods, it is the current release of wage-goods that determines the extent to which employment can be increased.

The principal aim of economic planning in an under-developed country is to raise the rate of investment and hence of capital formation with a view to an increasing flow of consumption goods in the future. Since there is a plethora of unemployed in the economy, the spending up of investment does not require curtailment of activities in the consumption goods sector; the economy can draw upon the reserve of unemployment. If concurrently with the increase of investment there is also increased production of consumption goods, as happens when there is excess capacity in the consumption goods sector, the wage-bill of the additional labourers can be met out of the additional output of consumption goods, and there is no pressure on the consumption goods market. We are, so to say, in the Keynesian world of plenty where an increment of investment leads by itself to an increment of consumption.

It is wrong to suppose that these Keynesian effects are altogether absent in an under-developed country such as India. The capacity in our organised sector does lend itself to fuller utilisation, as findings of competent statisticians indicate. Moreover the Plan period that we have in view is not exactly the Keynesian short period where resources and technique are given and fixed; certain investments may well be made to bear fruit during the Plan period. There is therefore some scope for the expansion of output of consumption goods to be set against the additional employment in the investment goods sector. But these possibilities are negligible in the context of the volume of investment that is needed to fully absorb the reserve of unemployment, when account is taken not only of the existing volume of 'disguised unemployment' but also of the addition to the labour force resulting from the normal growth of population.

Assume, then, to bring out the essence of the matter, that there is 'full employment' in the organised sector. What happens if, as the +

There is therefore no contradiction, as the authors imagine there is, between their theory of 'wage-goods gap' and the Planning Commission's 'logic' stressing the need for fixed capital. One refers to the short run and the other to the long run scope for employment. need for economic development demands, more employment is to be provided in the investment goods sector towards the production of capital goods? We are in the Classical world of Scarcity, and an adequate volume of wage-goods has to all, released from the rest of the economy to make provision for the additional labourers engaged in the investment goods sector during the investment period. The rest of the economy has to put up with reduced consumption, the extent of this reduction being determined by the wage-bill (assuming that wages are wholly spent on consumption) for the newly employed labourers. This is the raison dêtre of "saving" in the context of the economic development of underdeveloped countries, it is "saving" that makes possible an expansion of investment needed for the growth of the economy.

Now, the distinction between 'disguised unemployment' and new labour force generated in the process of population growth is often too sharply drawn. They are not necessarily distinct and separable entities. In practice, very substantially one merges into the other. The major impact of the growth of population in an underdeveloped economy is on agriculture. And there what happens, as population grows, is that an increasing degree of congestion occurs in the age group that call themselves 'occupied'. The 'saving potential' remains more or less the same, but the mouths to draw upon it increase in number. In fact, the distinction drawn here is not a distinction between two categories of unemployment; it is rather a distinction between two ways of looking at it. However, the distinction becomes analytically significant if we assume that the 'saving potential' gets released for use in the planned sector only at a level of employment beyond what would be needed for the full absorption of the newly emerging labour force. At any rate it is in this sense that the distinction is used here, although it is clear that there is no knowing in practice, at what level of employment this process of release of the 'saving potential' starts and when it operates, it does operate at all.

Since in the context of the situation that we are contemplating, additional employment is devoted entirely to Investment and is unaccompanied by any expansion in the
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output of consumption goods, the wages-bill of the additional labourers has to be matched entirely by 'saving' done in the rest of the economy. In so far as these additional labourers are recruited from the newly emerging labour force, the entire saving needed for meeting their wages-bill has to be newly created. It is only when investment is pushed so far as to enable the economy to encroach on the 'disguised unemployed' that some relief is found, on our assumption, in the release of goods that the labourers drawn into the planned sector used to consume in the subsistence sector. Even here, the 'wage unit' in the planned sector being substantially higher than the 'consumption unit' in the subsistence sector, further new savings have to be created for covering the gap.

All this becomes familiar story, when put in terms of money-wages and prices. An under-developed economy with a reserve of unemployed embarks on a process of planned investment. Additional employment is created in the investment goods sector. Payment is made to the labourers newly employed at the current money rate of wages. These wages are spent on the purchase of wage-goods. There is an increase in the aggregate-money demand for wage-goods. If, to start with, there is excess capacity in the consumption goods sector, output of wage-goods expands in response to the increase of demand, and there is no rise of prices, except to the extent warranted by the emergence of 'bottlenecks' here and there. If investment (and employment) is pushed beyond a level where excess capacity is fully exhausted, increased money demand presses on an inelastic supply of wage-goods, and prices start rising. The tendency is checked if the additional expenditure done by the newly employed labourers is offset by reduced expenditure elsewhere in the economy. The need for the offset is only lessened to the extent, that there is transfer of wage-goods from the non-monetized sector to the monetized sector where the additional expenditure has its impact. If therefore prices of wage-goods are, to be held constant in order for the real wage rate not to fall, the volume of additional (planned) savings needed in the monetized sector for the full absorption of the unemployed (disguised and undisguised) would be equal to the total money wages accruing to this entire body of newly employed labourers (assuming that wages are all spent; minus the money value of current prices of the increment of output of wage-goods, including the amount transferred from the non-monetized sector.

It is not difficult now to see the kind of hurdles that have to be got over in order for the economy to be able to utilise the 'disguised unemployed' for purposes of development. First, there is the problem, how to create conditions under which the disguised unemployed would get released from the subsistence sector and be drawn into the planned sector? Is wage incentive enough? If not, what organisational changes would be necessary for the purpose? Secondly, supposing that men are transferred, what guarantee is there that the goods that they were consuming would be transferred, too, to the planned sector? Is it not probable that those who would stay back would choose to retain at least a part of the consumption of the group that are switched on to the planned sector? The exodus of the 'disguised unemployed' will no doubt leave the subsistence sector with a 'surplus' of wage-goods. But those who will be still there will in all probability be reluctant to part with this surplus. This is partly because they will now wish to improve their standard of living and partly because they will have perhaps some more mouths to feed in view of a possible increase in the number outside the employable age group, as is likely to happen as population grows during the Plan period. What steps could be taken to prevent them from behaving that way? Will the normal price incentive be enough? Above all, thirdly, how are the necessary savings to be created in the economy, so as to cover the gap between the 'wage unit' and the 'consumption unit'? In an economy where normal savings do not take care of current additions to the labour force, this would appear to be the most serious obstacle to optimum growth, particularly when planning is conceived against the background of a democratic way of life.

Pressed with these considerations, our Planning Commission has chosen to go slow and has contented itself with making provision in their Second Five Year Plan at best for the current additions to the labour force, having to rely even there largely on deficit financing and foreign aid. Nobody, not even the framers of the Plan, will say it is an ideal Plan. But one has to have a sense of realism. It is no good just contriving an arithmetical jugglery and indulging in gratuitous criticisms, when the big socio-economic questions that the Commission is confronted with remain unanswered. We have to show the way to the solution of these before we take up the cudgel. Prof. Vakil and his colleague with their new-fangled 'consumption-goods multiplier notwithstanding, we have not done that.

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