CHAPTER I

INTRODUCTION

This study deals with the role played by agricultural prices in the process of economic development with stability. The theoretical analysis of the problem is followed by a case study of India's experience during the crucial fifteen years—from 1951-52 to 1965-66.

By economic development with stability, we mean first, that per capita output as well as aggregate output of the country in question will be steadily rising; secondly, in this process, the economy is not subject to such upheavals of prices as may worsen the standards of living of the masses and make for conditions which are inconsistent with a continuously rising rate of development.

The background of the problem dealt with in the thesis is that of an underdeveloped country which has set upon the

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1. I.M.F. Mission Report (1953) on India gives much the meaning to the term 'development with stability'. It says the test of any economic measure must be two-fold one—"...first, whether it will avoid deterioration in the present standard of living of lower income groups; second, whether it will encourage a steady growth of production that will make possible a rising standard of living in the future." See, "Economic Development with Stability," I.M.F. Staff Papers, Vol. III, No. 3. (Feb., 1954), p. 313.
task of developing its economy with deliberate efforts within the framework of a mixed economy. Because of such efforts, we may call these as developing countries as well, though their national output may not be increasing significantly.

'Underdevelopment' can be taken as referring to a low level of economic development, quite apart from the potentialities of the country concerned for further development. The term is a relative one and an underdeveloped country is "one which on the average affords its inhabitants an end product of consumption and material well-being appreciably inferior to that provided by the economies of the developed countries." Attempts have been made to compare the levels of standards of living in various countries, in order to indicate their stages of development. Such studies have shown marked disparity. Though per capita income is generally or broadly accepted as an indicator of the level of development, we have to remember that this is by no means a perfect


indicator and involves the assumption that income levels of the masses in general are reflected in the per capita national income figures. The main significance of low levels of living and incomes, as far our problem is concerned, is that any increase in income generates high consumption demand especially for food articles.

However, there is no such country which may be called, a typical or representative underdeveloped country. There is marked disparity among these countries with respect to levels of living, extent of industrialisation, structure of national income, the extent of state control, population characteristics etc. Benham adopts three principles to classify these countries — "... the degree to which they are over-populated, the extent to which they specialise on exports, and the extent to which their economies are controlled by their governments." The type of countries which interest us most here are the overpopulated countries, with export earnings constituting but a small portion of national income (so that we can conveniently assume a closed economy).

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and with their economies largely under private enterprise (especially agriculture). India is a major example of this type of countries.

The economic significance of over-population may be considered briefly for our purpose. The most important problem is that of increasing the rate of growth of national income sufficiently higher than the rate of growth of population, so that per capita income could improve materially. But this needs a high rate of savings and this is exactly what a higher rate of population growth makes it difficult to be achieved. Though a higher rate of growth of population exerts pressure on the demand side, it adds little on the supply side. Over-all shortage of labour as a limitation to economic development is nonexistent in these countries though there may be shortage of skilled labour. On the other hand, the problem is that of surplus labour and disguised unemployment to be found largely in the agricultural sector.

7. Several attempts to estimate the extent of this surplus labour, have been made. For example, D.M. Hanjundappa's estimate places the proportion of surplus working population among the farmer-families at 34.6 per cent in the five villages surveyed. Cf. D.M. Hanjundappa 'Community Development and Employment', Karnataka University, Economics Series - 2, Dharwar, 1963; pp. 27-30; Mujumdar's estimate of farmers affected by disguised unemployment is 71.4 per cent, and that of surplus labour is about 31 per cent. While Hanjundappa employs the first Quartile in the series of land-man ratios of actual holdings in respective villages as the norm for calculating surplus labour, Mujumdar uses the concept 'Standard Unit' allowing for variations in soil, climate etc. Cf. N.A. Mujumdar, 'Some Problems of Underdevelopment - An Analytical study of Underemployment in the Agricultural Sector', Bombay, 1961, p. 208.
However, the theory of zero marginal productivity of a substantial part of the population and the empirical evidence advanced in support have been challenged by several economists. The critics, however, forget an important qualification made to the concept by Hurkse. It is that only a major change in organization of agriculture can make the surplus population manifest. With a given technology and organization, a transfer of labour may reduce output.

Models of Hurkse, Lewis and Ranis-Fei focus attention on this surplus labour and view it as a savings potential which could be used to step up investment in the nonagricultural or capitalistic sectors. Two points need be mentioned here. Even if superior organization is established in the agricultural sector and surplus labour does emerge, it does not mean that any amount of labour could be transferred.


from agriculture whatever be the wage rate. An aggravating factor is the existence of organised labour in the non-farm sector which prevents wages from falling. The second point is, in the words of Vakil and Brahmanand, "whether the newly organised consumption sector can produce that surplus of wage goods which can provide the 'disutility' wage (wage equal to marginal disutility of work) to the unemployed so that all of them could be absorbed in investment activities." Two factors will prevent this process from becoming self-financing at the existing level of agricultural output. Increased per capita income in agriculture following reorganisation, would increase per capita consumption. Secondly, the disutility wage will be higher than the wage enjoyed by the surplus labour when they were on farms. Due to the existence of an organisation based on family system, the real wage enjoyed by the surplus labour on farms is not equal to marginal product but average product. A surplus of wage goods through an increase in agricultural output becomes necessary, therefore, for capital formation and industrialisation. This is so even if there is overpopulation in the urban sector also, making a transfer of labour from rural sector unnecessary or less necessary.

Khusro has shown that this would be the case in India for quite sometime to come.

The approach adopted in this study does not need the assumption of a population transfer. With limited resources at their disposal, the problem of underdeveloped countries is how to achieve a balance between considerations of capital formation and provision of consumer goods. The problem is whether and where to achieve balance between demand for and supply of goods in different sectors. This is because it is very difficult to recognize and obey the so-called sovereign consumer, and if balanced growth is to mean satisfying the freely expressed consumer demands for every good and service and that also in the short run, there can only be balanced stagnation and not growth. The point is, there are certain imbalances that can be tolerated and controlled and there are others which can neither be tolerated nor controlled. Agricultural imbalance belongs to the latter category.

This study seeks the explanation of inflation mainly in terms of the imbalance between agriculture and the rest.


of the economy. We shall see how this imbalance sets in an inflationary process which has more chances of being unstable, than of being stable, and how this mechanism of inflation has a dampening impact on industrialisation. This discussion will also show that imbalances in other sectors do not unleash such an unstable inflationary process and that increases in price level in other sectors do not have such serious implications for development effort.

Thus, the problem of balance between agriculture and the rest of the economy, the role of agricultural prices and the task of controlling them assume paramount importance in attaining the goal of economic development with stability. A study of inflation which concentrates mainly on the general price level, taking note of the sectoral prices only because they are constituents of the general price level and then seeking to explain the prices mainly through global monetary factors, cannot adequately depict the basic reality of the situation. The primary interest in this study is on agricultural prices, causal factors behind them, and their relationship with the general price level and economic development.

We have as a first step presented a theoretical model whereby we can visualise the nature of imbalances that may be created in a developing economy, and then study the mechanics and effects of instability generated therefrom.
This constitutes Part I of the thesis.

In Part II, after analysing the behaviour of different sectoral price levels in India as well as the relative price levels, we set about explaining this behaviour by relating them with important variables. Regression analysis is employed in explaining the variation in the prices of agricultural commodities, mainly food articles, and also the variation in the general price level. This enabled us to project the required production in the case of certain commodities such that targeted price stability is achieved. Impact of agricultural prices is then studied in terms of the effect on the cost of living, wages, other prices, savings and on the industrial sector. Of course, apart from the price behaviour, there are other factors which have an impact on the economy. In fact, these other factors have an impact on price behaviour itself, in addition to their impact on industrial climate and allied aspects of the economy. Import and export policy and tax policy are among

14. It may be mentioned that our primary attention is focussed on foodgrains, groundnut, sugarcane (ce), and cotton. Jute is not taken up for exclusive analysis because it is an export commodity and has not much relevance for the type of problem dealt with here. Plantation crops are also excluded. They form a category by themselves and stand apart from the traditional agriculture. Also, their significance in terms of consumer outlay on them relatively to other crops is limited. They also offer no scope for substitution with the rest of the crops.
such important factors. A detailed analysis of the role of such factors, however, lies outside the scope of this thesis.

Part III is devoted to exploring the effect of agricultural prices on the agricultural sector itself. The first issue here is how far the prices reach the farmers. Then, we study how far farmers respond to prices in terms of both production and marketable surplus. Difference is made between response in terms of aggregate agricultural production and substitution among different agricultural commodities. To the extent the rising prices reach the farmer and to the extent he positively responds to the price stimulus, the instability of inflationary process could be reduced.

Finally we are led to the policy implications, which are dealt with in Part IV. Price policy has two aspects - the role that it can play in removing the imbalance, which is a long term question; and secondly, the role that it can play in softening the impact of the imbalance, once it exists. In the light of the policy implications set out, we evaluate briefly India's agricultural price policy at the end.