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A Perspective on the Growth Process in India and China

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Abstract

In critique of the current growth process being experienced in India and China where inequalities have increased dramatically despite extraordinarily high growth rates, this paper argues that an increase in inequality is built into the dynamics of the system through the non-using up of their "labour reserves". Labour reserves continue to remain non-exhausted because at the rate of growth of labour productivity, which arises as a consequence of the shift in demand towards products that entail the use of technology with higher labour productivity, the rate of growth of labour demand does not adequately exceed the rate of growth of labour supply. The shift in demand itself arises from a shift in income distribution away from wages to surplus. Therefore, any growth strategy for India and China, if it is to address their social needs, must be one capable of rapidly absorbing their labour reserves. In this context, the author re-emphasizes the need for a growth strategy stimulated by an expansion of agriculture, which, in turn, must be based on non-expropriation of the peasantry from land.

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I

It is possible to argue that the growth rate figures for both India and China are exaggerated. But, we shall proceed by accepting them as correct. The inequalities in both economies however have increased dramatically during this very phase of extraordinarily high growth, to a point where substantial segments of the population, particularly, but not exclusively, belonging to the rural areas, appear to have witnessed little improvement in their living conditions, if not actual retrogression. This fact has been admitted by the governments in both countries. In China this admission was reflected in the call for a "socialist countryside" by the new leadership of the Communist Party in 2008, which entailed diverting substantial resources to the countryside for an improvement in the conditions of the people. In India the Eleventh Five Year Plan launched in 2007 aims at "inclusive growth", thereby admitting that growth till now has "excluded" large segments of the people.

Neither government however has been explicitly critical of the growth strategy pursued till now; both see high growth as the panacea for the conditions of the "excluded". In India in particular the emphasis is on still higher growth. The only theoretical "concession" made by the government has been to accept that the "benefits of growth" will not automatically "trickle down". "Inclusion" will require fiscal intervention by the government; for such intervention to work, however, a high growth rate is a necessary condition.

Whether India and China will continue to experience the growth rates they have been experiencing of late is a moot point. Both economies have become heavily export-dependent, with China even more than India, and the current world recession, if it persists, will certainly bring down their trend growth rates. But our purpose here is not to discuss the sustainability of the growth rate; it is to argue that inherent in the very nature of this growth process is a tendency towards "dualism" or a progressive accentuation in the internal social hiatus; an increase in the growth rate, far from eliminating or reducing this hiatus, may well accentuate it further.

This position is fundamentally different even from the "benefits-of-growth-will-not- automatically-trickle-down" point of view. It constitutes a basic critique of the growth process itself. If it is valid, and inherent to the growth process is a production of dualism, then no fiscal intervention by the State is likely to nullify it, as the Indian Eleventh Plan believes.

The obvious question that arises is: what exactly is meant by "this growth process"? After all, India and China have significant differences in their growth processes. Which is the common aspect of it that we have in mind in claiming that inherent to this growth process is a "dualistic" development? The immediate analytical answer to that question is: the flexibility of the product and process mix to adjust in response to changing market demand, in a situation where income distribution is largely market determined. In other words, the aspect being emphasized consists of two conditions: the fact that the production structure, and hence the ensemble of technologies adjusts to the pattern of demand; and the fact that income distribution, and hence this pattern of demand is itself largely market determined. These conditions characterize any capitalist economy. They obviously characterize contemporary Indian economy. And even in the case of China, they hold in substantial measure.

II

Poverty and abysmal conditions of life are necessarily linked to the existence of labour reserves. Many economists argue that the poor economies, like all economies, are characterized not by unemployment and underemployment but by low levels of productivity, and what is needed to overcome poverty is an increase in labour productivity. The difference between the "high labour reserves" view of poverty and the "low labour productivity" view of poverty may appear at first sight to be a merely semantic one; but there is a substantive difference, namely that the rate of growth of labour demand plays no role in the latter which sees interventions for overcoming poverty exclusively in terms of supply-side measures. (The current emphasis of the government of India on imparting skills as a means of overcoming poverty, on which more follows later, falls into this genre). Since labour demand in reality does play a crucial role, it is the non-using up of "labour reserves" which constitutes in our view the basic reason for persisting absolute poverty.

Now, there is a fundamental difference between India and China on the one hand and all the developed capitalist economies on the other, namely that the former are saddled with substantial labour reserves which cannot simply migrate abroad. This is a result of their colonial or semi-colonial past. Both China and India experienced "de-industrialization" in the sense of the destruction of their craft industries, and the throwing of large numbers of traditional craftsmen into the ranks of labour reserves that typically got located in agriculture, but also spilt over into low-paid occupations everywhere in the economy in the so-called "informal sector". W. Arthur Lewis calls India and China the locations of the world's labour reserves, but these enormous labour reserves did not always exist in India and China; nor were they the outcome of excessively high population growth rates as is often supposed. They got created as a consequence of colonial penetration into these economies, where, in addition to de-industrialization, the forcible introduction of a commodity economy in the context of an unpaid appropriation of economic surplus by the metropolis also played a crucial role. By contrast, today's developed capitalist economies not only never had such labour reserves to contend with, but even succeeded largely in exporting such labour reserves as they had, through emigration to the "new world" consisting of the temperate regions of White settlement.

It follows then that any growth strategy for India and China, if it is to address their social needs, must be one capable of rapidly absorbing their labour reserves. If this does not happen, then such a growth strategy necessarily sets up a vicious cycle. The existence of vast labour reserves keeps the real wage rate close to subsistence level. And the increase in growth rate, accompanied as it is by an increase in the growth rate of labour productivity, necessarily increases the share of economic surplus in the economy. An increase in inequality in other words is built into the system. Moreover, since those subsisting on economic surplus tend to demand newer goods which are in vogue in the metropolis, and which entail the use of technology with higher labour productivity, such an increase in inequality *ipso facto* gives rise to a further increase in the rate of growth of labour productivity in the economy, which again raises inequality, and so on.

In other words, a change in the structure of products and processes in the direction of higher labour productivity, which is itself in response to a shift in demand arising from a shift in income distribution away from wages to surplus, causes a further shift in income distribution, demand and technology in the same direction, since the labour reserves remain unexhausted. And the labour reserves remain unexhausted precisely because at the rate of growth of labour productivity that arises as a consequence of this dynamics, the rate of growth of labour demand, given the growth rate of output, does not adequately exceed the rate of growth of labour supply. We thus have a dynamics where labour reserves continue to remain unexhausted and the pauperized mass constituting the labour reserves continues to remain a pauperized mass; precisely because of the existence of such vast labour reserves, the wage rate remains tied to subsistence or near subsistence level. And yet the economy experiences extraordinarily high growth rates accompanied by extraordinarily high rates of growth of labour productivity, which both keep swelling the share of the economic surplus and get sustained by this very fact.

In presenting this picture we have assumed "given growth rate of output". That was merely a device for deferring a discussion of the factors that determine the growth rate. The dynamics sketched above, of a rise in the share of surplus giving rise to the demand for a change in the process and product mix, which calls forth technological progress leading to higher labour productivity, also calls forth investment and growth. In other words, the dynamics sketched above also spontaneously generates growth. But this spontaneous growth process can be deliberately accelerated through the pursuit of neo-mercantilist policies by the government or through the stepping up of public investment (or of public spending generally) as an exogenous stimulus.

State intervention, by way of both public investment and the pursuit of neo-mercantilist policies, has been far more pronounced in China than in India. In the latter, the quest for "fiscal responsibility" at more or less given tax rates, and the relative insignificance of net exports as a demand stimulus, have made growth largely a spontaneous affair, a fall-out of burgeoning capitalists', and more generally of middle class, consumption, sustained by a growing share of economic surplus.

Those in India who argue that the panacea for poverty lies in still higher growth of the same kind, usually see public investment in infrastructure as the instrument for stimulating higher growth, and this is what the Eleventh Plan visualizes. Their perception is normally a supply-side one, namely that public investment in infrastructure increases growth rate by removing bottlenecks on growth; but the importance of such public investment lies more in its ability to stimulate demand. To what extent the Eleventh Plan provides such a stimulus—given the government's quest for "fiscal responsibility" at more or less given tax rates, which is itself enjoined upon it by the economy's openness to speculative financial inflows—remains to be seen.

It is not our purpose in this paper, however, to discuss whether government intervention can accelerate the growth rate in an economy like India (we assume that it can in China), or whether, given the constraints upon the government, the growth process should be seen essentially as being spontaneous. Our argument is that even if the growth rate is accelerated, whether in India or in China, such acceleration may, instead of overcoming the dualism, further accentuate it. To illustrate this argument, we present a simple model.

III

There are two basic relations that we would emphasize: the impact of the rate of growth of surplus upon the rate of growth of productivity, and the impact of the rate of growth of productivity upon the rate of growth of surplus in an economy with labour reserves to start with. If μ denotes the share of surplus in output Q, which for simplicity is supposed to incorporate the outputs of both the modern and the traditional sectors, and θ the rate of growth of composite labour productivity, then the rate of growth of economic surplus, on the assumption that the real wage rate is given for the economy as a whole, can be written as $(g + \theta\alpha)$ where g denotes the rate of growth of output Q, and α is nothing but the ratio between the wage share and the surplus share, i.e. $(1-\mu)/\mu$. The rate of growth of labour productivity in turn would depend partly upon the rate of growth output itself, and partly, for reasons already mentioned, upon the rate of growth of surplus. Taking a very simple form of such dependence we can say that

$$\theta = cg + d\,(g + \theta\alpha)$$

Since the instantaneous rate of growth of employment at any moment is given simply by $(g-\theta)$, we can, by substitution, express it as: $g\,[1-c-d\{(1-c\alpha)/(1-d\alpha)\}]$. If this expression is less than the rate of growth of the labour force n, then the share of labour reserves at that instant of time will only increase.

The crucial parameter in this expression is d, i.e. the sensitivity of the rate of growth of labour productivity to the rate of growth in the size of the economic surplus. If it crosses a threshold level, then the term within the square brackets becomes negative. For instance, if $\alpha = 1$ to start with, then, even if we take $c = 0$, a value of $d \geq 0.5$ makes the term within the square brackets ≤ 0; for $c > 0$, the threshold value of d is lowered. If the term within square brackets is negative, then not only is a positive rate of growth in output accompanied by a negative rate of growth of employment, but an acceleration in the rate of growth of output is accompanied by a further increase in the negative rate of growth of employment.

If the term within square brackets is positive, then an increase in growth would appear to be beneficial, in so far as it reduces the magnitude of labour reserves. This is so even if at any given initial output growth rate, the relative size of the labour reserves keeps increasing, i.e. even if the rate of growth of employment, despite being positive, is less than the rate of growth of labour supply to start with. Even in such a case, an increase in the output growth rate will raise the growth rate of employment, in which case if output growth is raised to a sufficiently high level, then labour reserves will eventually have to diminish, as will absolute poverty, thus validating the claim of the government of India that the panacea for poverty is still higher growth.

But while this is perfectly true given the parameters of the above model, an increase in the growth rate—if brought about, as suggested by the government of India, through larger investment in infrastructure—cannot leave the value of c unchanged. The acquisition of scarce natural resources like land for infrastructure will certainly affect agricultural employment, so that an increase in the overall output growth rate brought about in this manner will be accompanied *ceteris paribus* by a higher rate of growth of labour productivity, thus amounting to an increase in the value of c. When this happens, then a rise in g will be accompanied by an increase in the value of the term within square brackets, in which case labour reserves will not necessarily get used up.

Of course, a question will be raised abut the term in square brackets, which denotes the instantaneous rate of growth of employment at any point of time divided by the growth rate of output. This term itself keeps changing over time, since α keeps changing over time as the share of surplus increases. As α tends to zero, the term in square brackets tends to (1-c-d), which is much less than when α is positive (since $c < d$). In other words, the dynamics that we have outlined above is only a transient phenomenon, in the sense that as the share of wages falls in output, the rate of growth of productivity tends to decline for any given growth rate. Sustained output growth, in the long run, is likely to generate a faster employment growth than initially. But this fact itself is of little consolation since the emergence of such dualism is likely to generate social tensions that make the arrival of the long-run itself rather problematical. The emergence of such dualism and its persistence even for some time will alter in other words the parameters of the model itself, so that we cannot claim a happy ending in the long run.

It follows that given the historical legacy from the days of colonialism of being saddled with massive labour reserves, which they have to absorb domestically, the growth process in countries like India and China—no matter how impressive in comparison to other countries, and no matter how effective in making them into budding "big powers"—does not really address their social need. It is not a matter, in other words, of growth rates; it is a matter of the growth process itself, because of which even an increase in the growth rate is unlikely to address their social need.

IV

A reference was made earlier to the view that the removal of poverty demanded an increase in the productivity of the labour force. Special emphasis is laid in this perception on the upgradation of the skills of the labour force. Some holding this view would argue that it is not an overall mismatch between demand and supply of labour that afflicts economies like India and China, but rather a situation of excess demand for skilled labour co-existing with an excess supply of unskilled labour. Others, who reject the idea of excess supply of labour altogether, would argue nonetheless that if the unskilled workers are given skills, then they will be able not only to access jobs, but also to do so at much higher wages than they earn as unskilled workers. In short, given the much higher wages that skilled labour gets in the advanced capitalist countries, at the prevailing level of wages of skilled workers in countries like India and China—which is much higher than their unskilled workers' wages—there is (for all practical purposes) an infinitely elastic demand for skilled labour. The way to overcome poverty therefore, apart from investing in the infrastructure sector, is to invest in skill impartation, including in education. The hype about China being the future manufacturing centre of the world and India being the future office centre of the world takes off from this perception. And the government of India's emphasis on higher education in the Eleventh Five Year Plan is also based on it.

While such emphasis on education is always to be welcomed no matter what the ostensible argument underlying it, since education enriches the human being, the specific argument mentioned above lacks validity. It is based on the presumption that the wage differential between skilled labour in the advanced countries and skilled labour in countries like India will induce a continuous shift of employment from the former to the latter, that capital is nation-blind. The fact that this has not been the case in history can scarcely be denied, for otherwise the dichotomy between the developed and the underdeveloped countries in world capitalism would never have arisen. But the proponents of this view would argue that capital is much more internationally mobile today than ever before, and that this mobility has introduced a nation-blindness into its perception.

Even if this was the case, the fact remains that during the entire long period since 1973 (the precise initial year makes little difference), the rate of growth of world output has been less than the rate of growth of labour productivity in the advanced capitalist countries. In the metropolis, the rate of growth of ex ante labour productivity is equal to the rate of growth of ex post labour productivity, since the unemployed exist more or less openly as unemployed. But this is not so in the developing world where the unemployed simply swell the ranks of "informal sector workers" and do not appear openly as unemployed, which lowers the observed rate of productivity growth below its "true value", i.e. what it would have been if the unemployed had been counted as unemployed. Hence the rate of growth of ex ante labour productivity in the developing world is necessarily higher than the rate of growth of ex post labour productivity. At the same time, the rate of growth of ex ante labour productivity in the developing world is higher than in the developed world, since the former like to catch up with frontier technologies which are much more advanced than what are in vogue in their economies. It follows from these propositions that the rate of growth of ex ante world labour productivity is necessarily higher than the rate of growth of observed labour productivity in the advanced capitalist countries, and hence, taking the world as a whole, the tendency in the post- "Golden Age" period, has been towards an increase in the relative magnitude of labour reserves, even in the absence of any population, and hence work-force, growth. The fact of a positive rate of world population growth has only worsened matters, though—unlike what is usually presumed—it cannot be held responsible for the fact that labour reserves are not getting exhausted at the world level. A shift of employment from the advanced capitalist countries to India and China in such a context would simply mean a redistribution of the world labour reserves, away from India and China to the metropolitan centres. This would mean a weakening of the home base of metropolitan capital, which it would not be able to afford for any length of time. And even if metropolitan capital is unmindful of the social and political consequences of such weakening in its pure quest for profits, the metropolitan capitalist States will put a stop to this weakening by restricting "outsourcing".

Hence, even though some amount of "outsourcing", whether of services or of manufacturing, is occurring at present and may continue for some time, there are strict structural limits to the extent to which it can be carried forward. And if the additional factor of the recession in the U.S., and over much of the metropolitan capitalist world is taken into consideration, then these limits will be reached even sooner. It follows that the "horizontal demand curve for skilled labour" hypothesis, as an argument for the view that the using up of the labour reserves is simply a matter of imparting skills to unskilled workers, lacks validity.

V

From what has been argued until now, it would appear that the only certain way for reducing labour reserves in countries like India and China is to follow any one (or all) of the following options: to intervene in the process of income distribution so that it ceases to be market-determined; to intervene in the process of demand formation by altering preferences (by debunking the hankering after metropolitan life-styles); or to snap the link between changes in the pattern of demand and changes in the process and product mix by controlling the production structure, as was the case in both these economies earlier. Of course if the last of these is given effect, then—since the impact of growth will be a reduction of labour reserves (as was the case in the former socialist countries)—inequalities in income distribution will be automatically kept in check, as the basic roots of such inequalities lie in the non-exhaustion of labour reserves. Hence a control over the structure of production, a regulation of the rate of technological change—so that this rate is not so rapid as to frustrate progress towards full employment—appears as the proximate intervention objective. It amounts, in terms of the above model, to a deliberate State effort to hold down the value of d, for which controls are the obvious mechanism. The problem with controls, however, is too well-known for recapitulation here. But there exists another way of reducing the value of d and hence achieving the same objective, which is both more efficacious and more acceptable. To discuss this we must introduce an additional element that has been missing from our discussion till now. We have so far talked of the economic surplus as one homogeneous mass; its distribution across different social groups has not figured in our discussion. But obviously, who earns how much of the economic surplus, or, if we move away from a pure "worker-capitalist" economy to one with petty producers, the distribution of income between the surplus earners on the one hand and the petty producers on the other, also has an important bearing on the pattern of demand, and hence the pace of technological change.

In particular, one can argue that even if the real wages of workers remain tied to the subsistence level owing to the existence of labour reserves, the terms of trade between agriculture and the other sectors (assuming that the relative prices between the secondary and tertiary sectors move more or less synchronously) will have an effect on the rate of productivity growth for any given growth rate: it will tend to lower both c and d and hence increase labour absorption. For the same reason, for any given subsistence real wage and terms of trade, a given rate of growth, if it is sustained more by the contribution of peasant agriculture, will have a larger labour-absorbing impact than if it is sustained more by the contribution of the other (capitalist) sectors.

It follows then that peasant agriculture-led growth will be far more labour absorbing than either export-led growth or consumption-led growth of modern sector products. (A situation of burgeoning exports of agricultural products, it should be remembered, is not the same as peasant agriculture-led growth, since such burgeoning exports can also be squeezed out of a stagnant agriculture; and peasant agriculture-led growth is not the same as agriculture-led growth, since the latter can be on account of corporate farming whose capacity to absorb labour reserves is limited for the same reasons as that of consumption or export-led growth of modern sector products).

VI

It was argued earlier that a mere acceleration of the growth rate does not necessarily entail a reduction in the relative magnitude of labour reserves. In the light of the argument just advanced, an additional variable has to be taken into account in our analysis, and this is the distribution of incomes between the peasants and even the small agricultural capitalists and proto-capitalists on the one hand, and the surplus earners in the modern capitalist sector on the other. While an acceleration of growth of the kind that India and China have been experiencing of late is unlikely to alleviate rural poverty (which may of course migrate to urban areas and thereby cease to exist as rural poverty), a deceleration of such growth, if accompanied by an adverse shift in the terms of trade for agriculture and other allied primary sector activities, will almost certainly aggravate rural poverty. It follows that during the period of recession in the world economy, rural poverty in countries like India and China will get aggravated for two distinct reasons: first, the slowing down of the growth rate as a result of it will reduce employment growth further below what it otherwise would have been (even if "what it otherwise would have been" might still not have meant a reduction in the relative size of the labour reserves); and second, the terms of trade shift against agriculture that such a slowing down of the world economy would entail will have a similar effect.

An important result of this would be an increase in inequalities within countries like India and China. This is for the following reason. A slowing down of growth in the metropolis will have contradictory effects on the diffusion of activities to countries like India and China. On the one hand, the cut in profits of firms will make them even keener to reduce costs by outsourcing activities to India and China; on the other hand, the growth of unemployment within the metropolis will make the metropolitan

States come down more heavily against such outsourcing. Some restrictions on outsourcing are likely, but only at the margin. The segment of the urban population that is a beneficiary of the current growth process is unlikely therefore to witness any significant cuts in its living standards compared to what it otherwise would have been, while the segment of the rural population that constitutes the "excluded" is likely to witness further deterioration in its living standards. A world recession therefore will compound both poverty and inequality in India and China, even though the booms they have witnessed may have been accompanied by increases in both.

VII

It may appear at first sight that the government of India's Eleventh Five Year Plan, which emphasizes a revival of agriculture, is aiming to do precisely what we have been arguing for, namely a peasant agriculture-led growth. But there are two basic differences: first, the emphasis on the part of the government is on "agriculture" and not "peasant agriculture" as such; and second, the means of stimulating a revival of peasant agriculture must include the provision of assured remunerative prices, and hence a commitment to the pursuit of appropriate exchange rate, trade and tariff policies which the government does not envisage; it talks instead of raising "productivity" to make agriculture "competitive". But if the rise in "productivity" is supposed to mean labour productivity, then the labour absorbing capacity of agriculture will go down; and if productivity is supposed to mean land productivity, then while the labour absorbing capacity may not go down, adequate incentives have to be provided for the introduction of land-saving methods, for which again a prior provision of assured remunerative prices constitutes a necessary incentive. Putting it differently, a strategy of peasant agriculture-led growth cannot be pursued within the context of a neo-liberal economy which allows freedom of financial flows (making any meaningful exchange rate policy elusive), which restricts the freedom to levy tariffs (though in India's case the actual tariffs on agricultural goods have often been below the tariff bounds), and which prioritizes the withdrawal of the State from market intervention.

To talk of “peasant agriculture-led growth” does not preclude egalitarian land reforms; on the contrary, precisely because a growth process based on a more egalitarian distribution of assets and incomes has a greater labour absorptive capacity than one based on inequalities, egalitarian land reforms must constitute a necessary accompaniment of peasant agriculture-led growth. Likewise, peasant agriculture-led growth does not preclude the formation of peasant co-operatives and collectives, including in the sphere of farming, as the basis for agricultural growth. In other words, peasant agriculture in this context does not necessarily mean individual petty production; it means agriculture based on a non-separation of the peasants from land, i.e. agriculture from which the peasantry is not expropriated (even if the impact of such expropriation is “softened” through the payment of some compensation or some price for their land). Since the labour absorptive capacity of any growth trajectory that entails such separation of peasants from land is likely to be low, such separation is likely only to end up swelling the relative size of the labour reserves.

The argument of this paper, in critique of the current growth process being experienced in India and China, may appear to some as similar to that put forward by Bukharin during the Soviet industrialization debate. While in some respects—e.g. the need for industrialization and, more generally, economic diversification in large “labour-surplus” economies like India and China, to be based on a home market provided by expanding non-corporate agriculture—there is a similarity between the two positions, the need for such agricultural expansion to be spearheaded by a burgeoning “kulak” class is not a part of what is being argued here. The evolution of the balance of class forces in the countryside and its implications for development, and hence conversely how a development strategy focused on the elimination of poverty should deal with it, is a separate matter that is not discussed in this paper. Its concern has only been to re-emphasize the need, in the context of economies like India and China, for a growth strategy stimulated by an expansion of agriculture, which, in turn, is based on a non-expropriation of the peasantry from land.