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CC-06 , Economics of growth and development - 1

Balanced and unbalanced growth

INTRODUCTION

In order to get rid of vicious circle of poverty, underdeveloped countries need investment on a large-scale.

There are two theories concerning strategy of economic development:

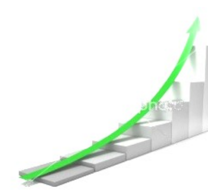
1.Theory of Balanced Growth: According to Rodan, Nurkse and Lewis, these economies should make simultaneous investment in all sectors to achieve balance growth.

2.Theory of Unbalanced Growth :According to Hirschman, Singer, Fleming, these economies should create a situation of unbalance by making large investment in anyone sector.

Theory of Balanced Growth

- *Fredrick List* was first to put forward the theory of balance growth. According to him, a balance could be established among agriculture, industries and trade.

- In the year 1928, *Arthur Young* gave the concept of different industries were mutually interdependent, then all of them should be developed simultaneously.



A strategy of growth with an equal emphasis on agriculture and industry. Agricultural development provides the food required and releases labour from the land to engage in industry. Industrial wealth stimulates markets for agricultural growth or such is the theory. Unbalanced growth denotes a strategy which focuses on agriculture or industry alone.

Definition

- According to Lewis

“Balance growth means that all sectors of economy should grow simultaneously so as to keep a proper balance between industry and agriculture and between production for home consumption and production for exports. The truth is that all sectors should be expanded simultaneously.”

Basis of Theory of Balanced Growth

1. Supply Side

Low Income ✉Low Saving✉ Low investment ✉Low productivity✉ Low Income✉---------

2. Demand Side

Low Income ✉Low Purchasing capacity✉ Low investment ✉Low productivity✉--------

Different Views Regarding Balanced Growth

1. **Explanation of Rodan's Theory of Balanced Growth.**

   According to an article 'Notes on Big Push'(1957) by Rodan, indivisibilities of supply side are concerned with social overhead capital. Indivisibilities of demand side means restricting the desirability and profitability of economic activities due to the narrow extent of the market.

   Rodan has referred to three kinds of indivisibilities:

(i) *Indivisibility in the production function or in the supply of social overhead costs*

(ii) *Indivisibility of Demand*

(iii) *Indivisibility of Supply of savings*

2. Explanation of Nurkse’s Theory of Balance Growth

According to Prof. Nurkse in the development of underdeveloped countries the greatest obstacle is Vicious Circle of Poverty. The Vicious Circle shows that income is low in underdeveloped countries. Because of low income, saving is low. There for investment and output is low. Low output means low income.

(i) Complementarity of Demand
(ii) Intervention by the Government
(iii) External Economies
(iv) Accelerated Rate of Growth

3. Explanation of Lewis's Theory of Balanced Growth

Lewis has given the following two arguments in favour of balanced growth:

(i) In the absence of balanced growth, price in one sector may be more than the prices in others.

(ii) When the economy grows then several bottlenecks appear in different sectors.

Balance among Different Sectors

- **Balance between Agriculture and Industries**
- **Balance between Human and Physical Capital**
- **Balance between Domestic Trade and Foreign Trade**
- **Role of Government in the Balance Growth**

Advantage of Theory of Balanced Growth

- ✓ Large size of Market
- ✓ External Economies
- ✓ Horizontal Economies
- ✓ Vertical Economies
- ✓ Better Division of Labour
- ✓ Better Use of Capital
- ✓ Rapid Rate of Development
- ✓ Encouragement of Private Enterprises
- ✓ Breaking of Vicious Circle of Poverty
- ✓ Encouragement of International Specialization
- ✓ Development of Social Overhead Costs

Criticism of Theory of Balanced Growth

This theory Criticized by Fleming, Singer, Hirschman and Kurihara.

- Unrealistic or Ignores Scarcity of Resources
- Ignores the Need of Planning
- External Diseconomies
- Development from Scratch
- Not a Theory of Development
- Same Policy for Developed and Underdeveloped countries
- Not supported by History
- Scarcity of Factors of Production
- Inflation
- Contrary to the Theory of Comparative Costs

Theory of Unbalanced Growth

Hirschman, Rostow, Fleming, Singer have propounded the concept of unbalanced growth as a strategy of development for the underdeveloped nations. The theory stresses the need for investment in strategic sectors of the economy, rather than in the all sectors simultaneously.

Unbalanced growth is a situation in which the various sectors of a given economy are not growing at a rate similar to one another

Specific sectors of the economy will be growing at a rapid rate, while other sectors are either stagnant or experiencing a significantly reduced rate of growth. When economic growth patterns such as unbalanced growth appear, the phenomenon usually indicates that major shifts in the overall economy are about to take place.

Explanation of the Theory of Unbalanced Growth

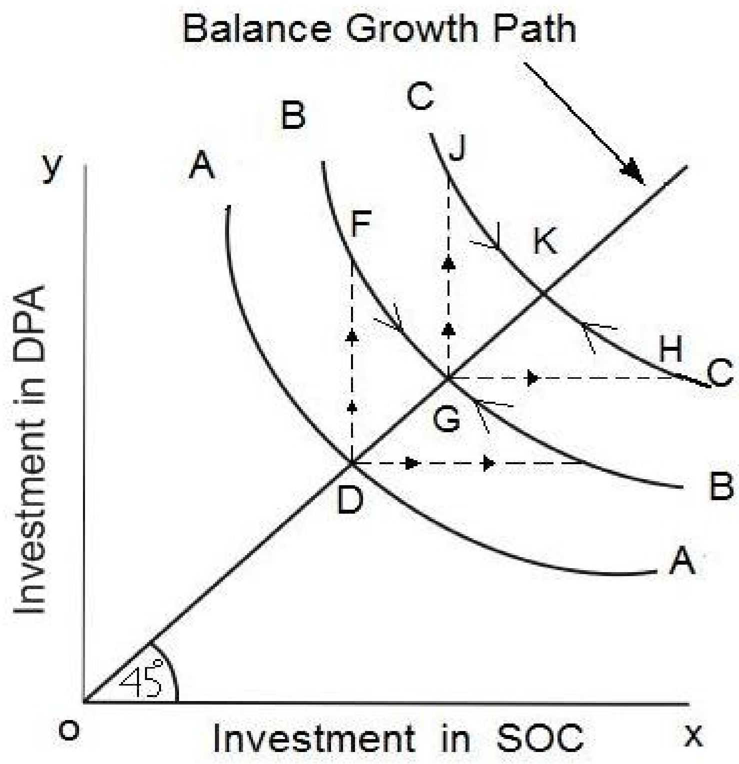
Prof.Hirschman states in his book,"Strategies of Economic Development", that creating imbalances in the system is the best strategy of growth.

Accordingly , strategic sectors of the economy should get priority in matters of investment:

- External Economies
- Compementries
- Social Overhead Capital or (SOC)
- Direct productive Activities or (DPA)
- Unbalancing the Economy through (SOC)
- Unbalancing the Economy with direct productive Activities(DPA)

Path of Development

- Development via excess capacity of SOC
- Development via shortages of SOC



Forward and Backward Linkages

1. Backward linkages
2. Forward linkages

Feature of the Theory of Unbalanced Growth

- Investment should first be made in the key sectors of the economy.
- Based on the principle of inducement & pressures.
- Big Push
- Real life observations
- Significance of the Public sector with regard to SOC activities

Merits of the Theory of Unbalanced Growth

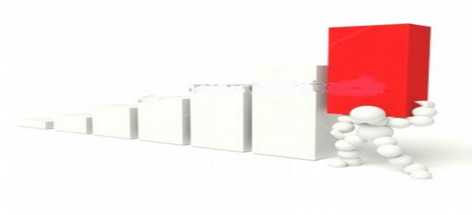
- ✓ Realistic Theory
- ✓ More Importance to Basic Industies
- ✓ Economies of Large Scale Production
- ✓ Encouragemence to New Inventions
- ✓ Self-Reliance
- ✓ Economic Surplus

Criticism of the Theory of Unbalanced Growth

According to Paul Streeten

- Inflation
- Wastage of Resources
- No Mention of Obstacles
- Increase in Uncertainty
- Unbalance is not Necessary
- Neglect of Degree of Unbalance
- Lack of basic Facilities
- Disadvantages of Localisation

Balanced Growth Theory Vs. Unbalanced Growth Theory



Balanced GrowthTheory:

1. Simultaneous growth of all sectors of the economy.
2. Seeks to accelerate the process of gowth through simultaneous investment across all sectors of the economy

Unbalaced Growth Theory:

1. Focuses is on the growth of certain key sectors of the economy
2. The process of growth through Imbalances in the system.

3. Requires lot of capital investment right from the beginning of growth process.

4. A long period of strategy of growth

5. Size of the market is the principal limiting factor.

3. Requires relatively much less investment.

4. A Short period strategy of growth.

5. It is decision making and entrepreneurial skill

Thank you