DEVELOPING BACKWARD AREAS
SOME QUESTIONS CONCERNING STRATEGY

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BACKWARDNESS, whether of large areas which constitute an entire economy or of smaller areas which constitute regions within an economy, has frequently been attributed to the paucity of resources—in particular the inadequate availability of capital.[1] There are a number of different variants of the theory, alternative models and formulations. But in substance these models and theories are reducible to what is commonly known as the 'vicious circle' theory. This theory argues that because the level of per capita income in backward areas is low the rate of savings is also low, a relatively high proportion of income being absorbed in order to maintain even a minimum level of consumption. And since investments must be financed out of savings, the rate of accumulation of capital is also low such that the growth of output is outstripped by the growth of population. The system therefore stagnates in this low level equilibrium trap.

RESOURCE CONSTRAINTS AND EFFECTIVE DEMAND

Alternative versions of the theory may sometimes stress the scarcity of factors other than capital, *e.g.*, labour in less populated economies, foreign exchange, entrepreneurship, etc. However it is always the inadequate availability of one or another 'crucial input' which is identified as the binding constraint on development. Accordingly it is argued that if only the missing input, or inputs, were made available then the backward area would cease to remain backward. Foreign aid then invariably turns up as the universal panacea, the means to acquiring the so-called missing input, a priceless magic potion that must be had no matter what its political and economic cost.

The only trouble with this otherwise attractive vicious circle theory is that it violates the simplest and most commonsense principles of demand and supply. Even the most conservative neo-classicist advocate of foreign aid would grant that where there is a critical shortage of some commodity, be it capital, labour or peanuts, arranging the supply of that commodity to

[1]See for instance G.M. Meier, "The Problem of Limited Economic Development", *Economia Internazionale*, Vol. VI, No. 4, 1953.

the backward area in question should turn out to be a profitable enterprise. In other words, given sufficient demand, if it is capital which is missing then the normal profit motives of the market should take care of it. Capital should flow into the backward area, attracted by the high price of capital. But this doesn't happen. Capital remains scarce.

The explanation of this awkward contradiction between fact and theory is simply that the theory of missing inputs is based on a false assumption, *i.e.*, the assumption that it is not the lack of effective demand but only the inadequate supply of some basic resource, especially capital, which is the villain of the piece. In fact, as Baran has pointed out in his penetrating analysis,[2] "the shortage of investible funds and the lack of investment opportunities represent two aspects of the same problem". Specifically in the Indian context, as Bagchi, Raj and many others have argued, in the present conjuncture of forces it is not so much the inadequacy of resources as the inadequacy of demand which is the operative constraint on our rate of capital accumulation.[3] There could of course be differences in the degree of severity of one constraint and the other between different regions. But in general it has to be recognised that it is not only the low level of capital accumulation[4] but also the low level of effective demand which operates as a barrier for the development of backward areas. Any strategy of intervention must, therefore, in order to be effective, not only ensure the growth of the physical capital stock in a given backward area but also the expansion of effective demand for goods produced in that area. And it is this impact on the double development constraint which must be taken as the appropriate test of a policy aimed at developing backward areas.

ECONOMIC BASE STRATEGY

Seen in the above perspective it is conceivable that the best possible means of developing a backward area is to identify the 'economic base' of the area and concentrate on the growth of these sectors. Drawing upon the fundamental theorem of the doctrine of comparative advantage in international trade, North, the original author of the 'economic base' theory,[5] argued that

[2]P. Baran, "On the Political Economy of Backwardness", *The Manchester School*, January 1952.

[3]See for instance, A.K. Bagchi, "Some Characteristics of Industrial Growth in India", *Econ. & Pol. Weekly* (Annual No.), February, 1975; K.N. Raj, "Growth and Stagnation of Indian Industries", *Econ. & Pol. Weekly* (Annual No.), February, 1976; S. Mundle, "Home Market, Capitalism in Agriculture and Drain of Agricultural Surplus", *Econ. & Pol. Weekly*, (Rev. of Agriculture), June, 1977.

[4]It is important to recognize that by accumulation we mean here the accumulation of a physical stock of investment goods.

[5]See D.C. North, "Location Theory and Regional Economic Growth", *Journal of Political Economy*, Vol. 63, June, 1959.

just as countries, no matter how backward, had to have a comparative advantage in the production of *some* commodities vis-a-vis the rest of the world, in the same way every region, however backward, had a comparative advantage in some commodities. These commodities are of course 'export sectors' in the sense that the large bulk of production was directed for export to other regions and perhaps even other countries.

It is evident that a strategy for developing backward areas can be formulated in terms of such economic bases or export sectors. For even if the level of local effective demand is too low to sustain rapid accumulation, profitable investment can still be sustained in those sectors which cater to external demand. And the export earnings accruing to the economic base should, operating through the regional income multiplier, lead to the development of the area as a whole.

Possibly some such process may have been at work in those regions of the United States which provided the evidence on which North based his theory. But whether in fact such a strategy of development will succeed in a particular case depends very much on the specific set of circumstances attendant to that particular case. For one thing regional economies are much more 'open' compared to national economies in the sense that a very large proportion of the local produce is usually destined for delivery outside the region while a large part of what is consumed within the region is delivered from outside. And while on the one hand export earnings generate expansion through the local income multiplier import payments constitute a symmetric leakage from the same multiplier circuit. Thus whether or not the export sector of a backward area can serve as an effective basis of development of the area depends very much on the net balance of trade of the area.

Furthermore, there is no guarantee that even a surplus balance of trade would necessarily lead to the development of a backward area. It is easy to see that the 'economic base' oriented strategy outlined above is nothing but the regional counterpart of the theory of export led growth of backward countries which is currently in fashion among a particular group of development theorists. However just like the 'shortage of capital' theory discussed earlier the theory of export led growth also stands in embarrassing contradiction to historical fact. The fact in question is of course the large and sustained export surpluses enjoyed by colonies vis-a-vis their metropolitan economies. In sharp contradiction to the theory, such periods of a surplus trade balance of the colonies appear to have coincided with the progressive *underdevelopment* rather than development of these colonies.

There is nothing really surprising about this because a surplus *balance of trade* could coincide with a deficit on capital account. And it is in fact such a sustained drain on the capital account which economic historians have consistently identified as the principal means of colonial pauperization of the Indian economy. Moreover, even when the balance of payments is so balanced that there is no net outflow of capital in the accounting sense, there may still be a substantial leakage of surplus from an underdeveloped country because of a fundamental undervaluation of its products imposed on it by an international market dominated by developed countries.[6] And as the modern theory of underdevelopment points out it is this leakage of the investible surplus which constitutes the very basis of the phenomenon of underdevelopment.[7]

The argument developed here applies just as much to the backward areas within underdeveloped countries as to the underdeveloped countries themselves. For the theory describes an entire hierarchical sequence of surplus drain within a single integrated international capitalist system. In this hierarchical structure surplus flows from the countries of the underdeveloped periphery to the developed metropolis. But within the periphery there are developed urban enclaves, satellites of the centre, which siphon off surplus from the surrounding backward areas of the hinterland. And within such a system it is easy to see that a strategy of backward area development which focusses on its 'economic base' would merely consolidate the mechanism of surplus drain. Financial and other assistance to agricultural or industrial entrepreneurs (depending on which sectors in the region enjoy comparative advantage) would certainly lead to some growth in the 'export sectors' of the area. But the additional surplus would simply get siphoned off, leaving the area as a whole as backward as before.

Recently an interesting variant of this general dependence model has been formulated by Chattopadhyay and Raza to specifically explain the perpetuation of backward areas and regional disparities within the Indian economy[8]. Arguing that colonialism merely welded on capitalist modes of surplus generation, appropriation and utilization to the pre-capitalist modes rather than *replacing* the latter, *i.e.*, that it introduced the Prussian or 2nd path of capitalist development rather than the more progressive American path, Chattopadhyay and Raza contend that this gave rise to a certain conglomerate form of property which effectively blocks the development of backward areas.

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[6]For a systematic exposition of the theory of exploitation through trade see A. Emmanuel, *Unequal Exchange, A Study of the Imperialism of Trade*, New Left Books, 1972.

[7]See among others P. Baran, *The Political Economy of Growth*, Monthly Review Press 1957; A.G. Frank, *On Capitalist Underdevelopment*, Oxford University Press, 1975; S. Amin, *Accumulation on a World Sale*, Monthly Review Press, 1974.

[8]B. Chattopadhyay and M. Raza, "Regional Development: Analytical Framework and Indicators", *Indian Journal of Regional Science*, Vol. VII, No. 1, 1975.

"So long as the economy does not break out of the premises of capital accumulation characteristic of the 2nd way—that too in the context of colonial legacies—even directed public investment cannot deliver the goods. For, the benefits of the external economy—effects of such investment—will be mopped up and impounded by the urban and rural *conglomerates.*

"*Conglomerate property* is the specific form that titles to income and wealth assume under conditions of coalescence of the several modes of generation, appropriation and utilisation of surplus in agriculture and industry promoted by the State. Its characteristic feature is that it spreads out its assets over a wide range of activities embedded in different modes of appropriation of surplus in such a way that the quickest and surest returns are ensured.... The consequent investment preference will inevitably prompt such conglomerate property to gravitate toward the already developed pockets—the urban agglomeration and the high incentive rural pockets and crops. Conglomerate big business in the organized urban sector will, therefore, thrive in the urban agglomerations and conglomerate large landholdings will thrive in the Package District pockets, thereby accentuating the built-in structural dualism and disparities of the inherited space economy." (Chattopadhyay and Raza 1975).

VARIANTS OF ECONOMIC BASE STRATEGY

Support Prices

A possible solution one may think of in this context is to develop the products of comparative advantage in a backward area for export to other regions along with a support price policy to ensure that the surplus does not leak out along with export. But even this policy is unlikely to help. First of all unless the product is exclusively produced in the area in question, a policy of price support would entail support for the commodity not in one region alone but throughout the national market. For it is not feasible to maintain different prices for a single commodity in different regions within the same national market, especially when the commodity is an export item absorbed mainly outside the region of origin. Thus unless a support price policy for the commodity is required by considerations of the national market it is not possible to execute such a policy locally for a single backward area.

Moreover even if such a policy of price support for the local exportables could be successfully implemented, this alone would not ensure retention and investment of the resultant surplus. We have seen earlier that in order to be successful, a policy for developing backward areas must not only provide resources for investment but also generate demand within the region. Without this, surplus would continue to find its way elsewhere where the rates of return on investment are higher. And since the export-with-price-support strategy can do little to generate such local demand it would do no more than link up the export sector with the urban-industrial enclave without altering in any way the backwardness of the area as a whole.

Industrial Estates

The argument developed above tries to explain why a policy of financial support to private entrepreneurs to develop the export base of the backward area is unlikely to succeed—even when coupled with support price policy. A slightly different approach to the problem is the building up of industrial estates. The strategy here is to channelise public resources not only towards financial assistance of private entrepreneurs but also towards building up a wide range of infrastructural facilities such as power, roads, factory sheds, etc. Through the build-up of this complex of facilities which would generate very substantial external economies for potential industries, cost curves are sought to be brought down such that investment in the area becomes more profitable. In principle, creation of such external economies could be expected not only to check the flight of surplus to more developed regions but even attract capital from outside. In accordance with this logic it became one of the central objectives of the industrial estates programme in India "to use the medium of industrial estates for dispersing industries to rural and under-developed areas in order to raise their levels of improvement".[9] The industrial estates programme in India was started during the First Plan and subsequently grew through the later plans into one of the largest industrial estates programmes in the developing world.[10] While some estates were planned for developed urban and semi-urban areas where the necessary infrastructure already existed, others were planned for backward rural areas where the necessary facilities would have to be newly developed. However as the programme proceeded it turned out, as a Parliamentary Estimates Committee (1966) pointed out, that a large number of urban estates were a thumping success, but the performance of the rural industrial estates was in general quite indifferent.[11] Closer scrutiny revealed that among the rural industrial estates those which already had certain inherent advantages—especially in terms of access to markets and raw materials—became viable while those

[9]See Central Small Industries Organization, Ministry of Commerce & Industry, *Industrial Estates: Programmes and Progress*, p. ii.

[10]For analytical accounts of the programme see among others P.C. Alexander, *Industrial Estates in India*, Asia Publishing House, 1963; and P.N. Dhar and H.F. Lydall., *The Role of Small Enterprises in Indian Economic Development*, Asia Publishing House, 1960.

[11]See, V.S. Vyas, *Rural Industrialisation: An Integrated Approach*, Karnataka University, Dharwar, 1971.

located in backward areas which had inherent disadvantages failed.[12] In other words a programme of investing in infrastructural facilities alone was not enough to compensate for the inherent disadvantages of a region, in comparison to other regions, which resulted in its remaining *or even becoming* backward in the first place.

The reasons for this are not difficult to identify. We have seen at the outset that in order to be effective a strategy of developing backward areas must not only release the resource bottleneck but also the demand bottleneck. Now the expansion of physical capital in the form of infrastructure is certainly a relaxation of the resource bottleneck. The creation of such resources generates externalities which could push down cost curves for industries were they to be located in the area. Furthermore if the industrial estate is of a *functional* type,, *i.e.*, aimed at industries of a particular type or types in which the area has a 'comparative advantage', then this is tantamount to using the economic base strategy discussed earlier which is again an attempt to tackle the problem from the side of resource availabilities. But none of this takes care of the demand bottleneck. And as in the case of the other strategies examined above, the lack of adequate effective demand *within* the region swamps any process of self-sustaining growth which an industrial estate may have otherwise catalysed in the backward area.

Large Industrial Projects

Though a strategy of developing industrial estates of the *functional* type failed to recognize the demand problem in backward areas, an alternative form of industrial estate policy has been tried which is clearly designed with a view towards tackling this problem. This is an industrial estate of the *ancillary type*. Here instead of concentrating on a single industry, the estate is designed to accommodate a number of small industries of different varieties which are supposed to function as ancillaries to a major industrial project located nearby.[13] The idea seems to be that the major industrial project located in a backward area will provide the demand pulls for all round development of the area. The ancillaries are supposed to be the conduits through which the growth impulses will be dispersed in the area. It is easy to see that in contrast to the earlier case, in this case it is not the industrial estate itself but the major industrial project which is supposed to function as the principal engine of growth—the economic base—of the area. This strategy once again has been widely experimented within the Indian economy, but the impact of

[12]On this see the interesting comparative study of the estates at Saktigarh and Baruipur in Bengal in Kalyani Bhattacharya, *Industrialisation through Industrial Estates*, Bookland, Calcutta, 1969.

[13]See, K. Bhattacharya, *Industrialisation through Industrial Estates*, Bookland, Calcutta, 1969.

such massive industrial projects on the local backward areas appears to have been negligible, if not actually adverse.

It has been estimated that the employment potential of such large units works out to only 4 persons per one lakh rupees of investment. In addition even out of the small number of persons employed a large proportion has to be recruited outside because appropriately skilled persons are not available within the backward area.[14] An identical problem occurs in the case of producer goods. The investment and intermediate goods demand of these large units are so sophisticated that local ancillaries are incapable of meeting such demand. Consequently a large bulk of the producer goods feeding into the large industrial unit also comes from outside the backward. In other words, just like the 'comparative advantage' based export sectors discussed earlier, the large industrial unit merely becomes another enclave which has little relationship with the surrounding backward region. As the large number of giant projects in Orissa, Madhya Pradesh, Bihar and elsewhere have shown, they certainly do not generate the kind of demand impulses which would pull the surrounding hinterland out of backwardness and launch it onto a path of self-sustaining growth. On the contrary it has sometimes been argued that the introduction of a major project, while it leaves the distant hinterland quite unaffected, does disrupt the traditional occupation and economic and social life in the immediate neighbourhood. And this happens without much compensating expansion of local employment and incomes. The net consequence is that apart from the small and fortunate minority who are absorbed into the unit, the rest of the destitutes population becomes even more destitute than before.[15]

LABOUR INTENSIVE PUBLIC INVESTMENT

We started out by arguing that a policy of merely pumping in resources was unlikely to pull a region out of its backwardness because the origin of such backwardness lay not only in the paucity of resources within the region but also in the low level of demand which precluded the possibility of profitable investments catering to the local market. Consequently any strategy of intervention would succeed only if it released at the same time *both* the resource constraint and the demand constraint. In the light of this criterion we examined the viability of the 'economic base' strategy, a staple of conventional regional development theory, as well as some of its variants. And it turned

[14]These characteristics of the large unit strategy in backward areas were recently highlighted by the Industries Minister in his reply on budgetary demands of his Ministry. See *Times of India*, July 12, 1977.

[15]For a case study of the Bokaro Steel plant and its impact on the local Bauri community see N. Sengupta, *Destitute and Development: A Study of the Bauri Community in Bokaro Steel Region*, A.N.S. Institute of Social Studies, Patna, 1976.

out in each case that the strategy was inadequate because it failed to ensure a sustained expansion of local demand within the backward area. And this failure would have a feedback on the resource problem as well since the lack of profitable investment opportunities would not only not attract private resources from outside but it would actually lead to the leakage of whatever little private investible surplus is actually generated within the region.

From the foregoing review it is possible to derive a number of straightforward conclusions. Since private investment considerations would siphon resources away from a backward region rather than attract resources from outside, it is evident that at least till such time as the nature of investment opportunities and profitability is fundamentally altered in the region investment would largely have to take place in the public sector. Secondly, if these investments are concentrated in sophisticated industries where supply and demand links are mainly outside the region then by their very nature these industries would become enclaves which have little or no effect on the region as a whole. In other words public investments would have to be of such a nature that they help *create* a growing local market. However, if the demand created through public investment is mainly for highly processed inputs rather than labour then this again would fail to effectively catalyse the growth of the region since there would be no potential for meeting such demand locally. Public investment would therefore have to be concentrated in projects with a high employment potential. If the employment generated by such investment is sufficiently large, it would immediately expand the purchasing power of the region and create a substantial market, even if only for consumption goods, *within* the backward area. To the extent that such demand can be met locally, *e.g.*, foodgrains and other agricultural products, this would directly lead to an expansion of production in pre-existing activities. Where even such demand has to be met from outside the region initially this would at least attract merchant capital from outside. And competition between traders bringing in goods from outside should ultimately lead to productive investment in simple processing and manufacturing of consumer items inside the area itself. Once this stage is reached, the fundamental alteration of investment opportunities referred to earlier has occurred. And after a point the region should be capable of sustaining its own growth even without a special thrust of public investment.

What we have just done in effect is to outline a strategy of backward area development which simultaneously takes care of the *double* development constraint. This is the strategy of sustained public sector investment in labour intensive projects. Such a strategy not only brings in resources to the backward area but simultaneously creates a substantial consumer goods market *within* the region. And as we pointed out at the outset it is only such a strategy which releases both the resource bottleneck as well as the demand bottleneck which can effectively pull a region out of its backwardness. But the crucial element in this strategy is that public investment must be *sustained* over a fairly long period.

Indeed there is nothing new in a policy of large scale public expenditure on employment oriented schemes. Paying people if only to dig holes and fill them up again is an aphorism deriving from no less a person than Keynes himself. But Keynesian employment policies were short-term measures situated in developed and on-going market economies caught up in a temporary depression. Employment oriented public sector programmes for backward areas in developing economies are qualitatively different in the sense that they must be long-term programmes. Following the work of Nurkse[16] and many others labour intensive capital building projects were launched in India and elsewhere. As a means of converting abundant and cheap labour into scarce and highly valuable physical capital such projects were undoubtedly invaluable. But precisely because such projects were conceived from the point of view of getting round the resource constraint rather than the demand constraint, they often turned out to be short run one-shot attempts. Once a project was completed in a particular backward area, the region would more often than not settle back to its pre-existing subsistence level of income and employment.

The same lack of sustained employment opportunities seems to have characterised many of our experimental employment schemes of the early seventies such as C.S.R.E., P.I.R.E.P. and the famine relief programmes in drought prone States.[17] This is why the employment programmes have so far failed to achieve any significant break-through in pushing up income levels in impoverished pockets. And this is the crux of the problem. Even labour intensive public investment projects will fail to pull a region out of its backwardness unless such projects are capable of *sustaining* employment, income and local demand until the economy of the region experiences that fundamental transition from a surplus repelling area to a surplus attracting one. The identification, planning and management of such projects seem to be among the most challenging tasks of development confronting us today.

[16]See R. Nurkse, *Problems of Capital Formation in Underdeveloped Countries*, Basil Blackwell, Oxford, 1955.

[17]For an analysis of such programmes see S. Mundle, "Relief Planning in Maharashtra", *Indian Journal of Public Administration*, Vol. XX, No. 4, October-December, 1974.