VICIOUS CIRCLE OF POVERTY AND THE SCARCITY OF CAPITAL

(It is a widely held notion that many Third World countries, particularly the countries of South and South-East Asia and Africa have been caught in the 'vicious circle of poverty'. GNP per capita has remained almost unchanged for decades, and in some cases for the past two-three centuries, mass of the population in these countries has lived under sub-human living conditions, whereas, only a microscopic minority having control over the means of production enjoyed all the luxuries. Indian people, for example, underwent this experience under the British rule.) Writings of Dadabhai Naoroji and R.C. Dutt bear testimony to this fact. Even the national income estimates of Surendra J. Patel, K. Mukerji and Arora and Iyengar for the first half of the 20th century support the view that there was virtually no economic progress in India during the last five decades of the British rule. No doubt there was some infrastructural development and a few industries were also set up, yet in terms of per capita income it was definitely a period of economic stagnation. It is not difficult to get similar evidence from other countries also giving credence to Nurksian theory of vicious circle of poverty.

Vicious Circle of Poverty — Its Implications for Economic Development

Let us now consider the concept of vicious circle of poverty and its implications for economic development. Most economists, who find reference to the colonial past of the Third World countries rather inconvenient, blame the rampant poverty in these countries for their inability to develop. The foremost among them is Ragnar Nurkse. His book *Problems of Capital Formation in Underdeveloped Countries* is one of the best known on this subject. It has exercised considerable influence on thinking in the developed and underdeveloped world alike. Nurkse summarises his theory as follows:

"In discussions of the problems of economic development, a phrase that crops up frequently is the **vicious circle of poverty...**

"**It implies a circular constellation of forces tending to act and react upon one another in such a way as to keep a poor country in a state of poverty.** Particular instances of such circular constellations are not difficult to imagine...

"Perhaps the most important circular relationships of this kind are those that afflict the accumulation of capital in economically backward countries. The supply of capital is governed by the ability and willingness to save; the demand for capital is governed by the incentive to invest. A circular relationship exists on both sides of the problem of capital formation in the poverty-ridden areas of the world...

"The low level of real income, reflecting low productivity, is a point that is common to both sides."[1]

Nurkse's argument apparently looks convincing. **When a country is poor, its ability to save is quite limited.** Extremely poor countries rarely save more than 10 per cent of their national income and inevitably face shortage of capital for developmental activities. Scarcity of capital also dictates the use of labour-intensive technology as a result of which productivity levels remain low. Low productivity levels both in agriculture and industry neither provide economic surplus for raising the investment level, nor leave so much disposable income to households that may raise their consumption standards. Thus, thinking along Nurksian line one gets convinced that there is little that poor countries can do to overcome their present-day poverty. Long ago Samuelson had also argued on the same lines. In the second edition of his famous textbook, entitled *Economics: An Introductory Analysis*, he wrote, "They (the underdeveloped countries) cannot get their heads above water because their production is so low that they can spare nothing for capital formation by which their standard of living can be raised."[2]

Vicious circle of poverty hinders economic development from the demand side of the capital as well. In a poor country, the size of market is small, and as a result inducement to invest is missing. Small investment activity implies low level of output which ultimately results in widespread poverty.

Factors Keeping Rate of Capital Formation Low

Let us now examine the factors which have prevented many Third World countries from raising the rate of capital accumulation, a necessary condition for both initiating the growth process and then accelerating it. **In almost all underdeveloped countries, feudal relations of production co-exist with capitalist relations of production. Presence of feudal or semi-feudal relations of production prevents technological changes in agriculture.** Keeping multitudes of peasantry in abject poverty, feudalism does not leave any resources with

INAPPROPRIATE TECHNOLOGY

The second major obstacle to development in Third World countries is their reliance on inappropriate technology. These countries have either low productivity technology which fails to generate much economic surplus or in certain sectors they have highly sophisticated imported technology with low labour absorption capacity. In any case, none of these technologies are best suited to the requirements of developing countries.

1950s. A classic study by Sol Tax, *Penny Capitalism*, pertains to a Guatemala village Panajachel. Sol Tax clearly shows that in spite of the fact that the people of Panajachel make the most of the factors and techniques of production at their command, they are very poor. Hence, 'remarkable efficiency' on the part of the people in allocating the small amount of factors at their disposal is of little help in forcing the pace of development. Their inability in this regard is primarily caused by their backward technology coupled with the scarcity of capital.[8]

Imported Technology

The other technology which Third World countries now use is the one which they have imported from developed countries. It is something which has been dictated by the historical development of technology. Over the past 150 years whatever technological developments have taken place, have all been concentrated in advanced countries. Obviously these techniques were developed in response to the needs of these countries and do not necessarily suit the requirements of the present-day developing countries. However, having failed in developing their own technology, Third World countries have now little choice except to import technology from advanced countries. Often developing countries buy second-hand machinery from advanced countries. This sometimes enables them to set up certain industries or develop infrastructure, but it rarely helps in improving their competitive power in international markets *vis-à-vis* advanced countries. The latest techniques in use in the West are highly sophisticated. As they are all highly capital intensive, they are likely to displace labour and thereby increase unemployment in the already labour surplus economies of the Third World. In most of the developing countries, while labour is in abundant supply, capital is scarce. Hence, the more recently developed techniques imported from developed countries might not serve much purpose in most of the developing countries. It is true that in the developing countries there will always be certain sectors in which use of the most sophisticated technology will be decisively advantageous. Schumacher, however, asserts that these sectors will never account for more than 15 per cent of the whole economy. For the remaining 85 per cent of the economy, he recommends what is now known as intermediate technology. **In his opinion, intermediate technology is superior to declining traditional technology of the developing countries and is also more appropriate than the imported technology of the developed countries.**[9]

POPULATION EXPLOSION

Population explosion is a concrete reality in Third World countries which are at present passing through the second stage of demographic transition. In all these countries, mortality rates have suddenly fallen without a corresponding decline in birth rates. Some of the less developed countries now find themselves in a very difficult situation as their gains from development are being lost on account of population growth.

population in a less developed country, it is not conducive to development.[12]

Cassen asserts that rapid growth of population does not permit any positive change in occupational distribution of population in a backward economy as long as employment generation remains an important objective of economic policy. Since the problem of unemployment is already very serious in Third World countries, they can hardly pursue a policy whereby it increases further. Cassen thus contends that rapid population growth in these countries "postpones the transformation of traditional economy into one dominated by the manufacturing sector. This is not only because of the agricultural requirements of growing numbers, but also because of the relative investment costs of job creation in agriculture and manufacturing."[13]

Political Obstacles

In modern theories of development and underdevelopment role of political factors has been underplayed. Rarely an economist refers to them, and in case anyone chooses to do that, he too treats political factors as if they are of little consequence to the development of an economy. The fact, however, remains that it is not possible to explain the present-day underdevelopment of most of the countries in Africa, Asia and Latin America correctly without reference to their political subjugation by the West. Even now when these countries have managed to get political freedom, their political system is still operating as a major obstacle to their development. **In a large number of the Third World countries there is no political stability.** Governments are frequently changed by political machination and military coups. Often the imperialist powers also do manoeuvrings to destabilize governments in the developing countries. This whole political atmosphere is not at all congenial to development. Even in countries where political system is stable, the rulers represent the interests of the propertied classes. In Brazil, Mexico and Indonesia, for example, there has been no political turmoil for quite some time. The governments in these countries have been in complete control of the situation; yet in all these countries poverty, unemployment and income inequalities have increased. No doubt in the recent past some growth did take place in these countries, but its gains have been completely appropriated by the elites whose interests these governments serve. In the Middle East, fundamentalist governments have virtually no commitment to development. Pursuing revivalist policies, these governments are not in the least forward looking. To be brief, the authoritarian regimes in developing countries have neither the necessary commitment nor the required capacity to pursue any programme of economic development. Wherever democratic governments have been set up, some attempts have been made to force the pace of development. But even in these countries development performance cannot be regarded as very satisfactory. In India, for example, political system is not as fragile as in most of the Afro-Asian or Latin American countries. The form of government is democratic based on universal franchise. Nonetheless the influence of not only capitalists, traders, landlords and kulaks but also of communalists and fundamentalists is all pervasive and has proved to be a serious obstacle to development.

Administrative Constraints.

Most of the developing countries have retained the administrative machinery which was created by their foreign rulers in the colonial period. This administrative machinery is inefficient and lacks ethical values. Therefore, it is not at all surprising that **corruption and red-tapism are deep rooted in the government administration.** In Third World countries the administrative machinery which was created to exploit the native population by the foreign rulers is now being used for developmental purposes. Obviously the confidence which is often reposed in it is misplaced. One can easily notice the administration's negative contribution in those countries where State enterprises have been assigned the role of a leading sector within the basically capitalistic framework of the economy. In some of the developing countries large public sector has been developed. Though its contribution to development is not small, yet it must be admitted that the performance of most of the public sector enterprises is far from satisfactory. Their failure is often rightly attributed to [illegible] and corruption of management. System of industrial licensing, import

SOCIO-CULTURAL OBSTACLES

Often underdevelopment in Third World countries has been attributed to their socio-cultural fabric reflecting their values, motivations, attitudes and incentives. Religion in these countries has seldom played a positive role. Putting on the cloak of spiritualism it has not only legitimised exploitation, but has also proved to be a barrier to development. Similarly casteism and tribal loyalties do not seem to have any merit from the point of view of economic development. Generating unnecessary tensions among the various sections of the population these divisive forces create such conditions in the society which are inimical to development. However, it would be wrong to exaggerate the role of social and cultural factors in influencing the rate and pattern of development in any society, though some development economists and economic historians have been tempted to explain the poverty and backwardness of a number of communities in terms of prevailing social attitudes and institutions. For instance, Vera Anstey, L.C.A. Knowles and many others have explained India's economic stagnation during the colonial period in terms of cultural traits. Contempt for manual labour among the high caste Hindus and the institution of joint family have been particularly blamed as they supposedly discourage productive effort among a vast section of the society. It seems that these economic historians have exaggerated the negative role of social attitudes and institutions in Indian society. However, as noted by Leon Mears and Adamantios Pepelasis, it "can be argued legitimately that in some societies certain values and institutions appear to be unconducive to the promotion of economic progress precisely because the economies of these societies are backward. That is, cultural forces do not necessarily exert a directly retarding influence on an economy; they simply mirror a relatively low level of economic development."[15]

Marxists are of the opinion that views and institutions do not come into being and develop independently. They correspond to the material base and serve its consolidation and development. Thus, attitudes and institutions are a powerful active force in a society and in an otherwise retrogressive society their negative contribution to economic progress may be substantial.[16] The impact of social institutions and cultural values on economic progress is constraining in so far as these values represent deviations from rationality. Irrational behaviour tends to persist even when national pressures exist. Interestingly irrationality is not easy to deal with because its hold creates strongholds of vested interests which shape political institutions, social customs, communal norms, etc.

Let us now consider how religion, caste and family ties become barriers to development. According to Max Weber, cultural values, social structure, personality and motivation come together in any religion. Once religion is defined in this manner, it becomes easier to appreciate its negative role in economic development. Commenting upon the impact of religion on Indian life, Vera Anstey has succinctly remarked, "The religious attitudes, no matter what particular creed is involved, pervades every sphere of life in India, and tends (as it has invariably tended, in all ages and climes, when it has governed secular life) to engender rigid traditionalism and conservatism, and to present unreasoning opposition to every innovation, however enlightened and humane. Religion excludes the economic motive, and replaces it by the ideas of custom and status. The

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falls to ...

EXTERNAL BOTTLENECKS

Economic relations between the developed capitalist countries of the West and the less developed countries of the Third World are now proving to be a major barrier to economic development of the latter. The classical theory of trade has been used by economists for a considerable period of time to argue