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ECONOMIC DEVELOPMENT AND INCOME DISTRIBUTION IN UNDERDEVELOPED ECONOMIES: AN OVERVIEW

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The General Picture

All available data on income distribution in underdeveloped economies show a clear-cut and uniform pattern. That is to say, the pattern of income distribution in such economies conforms to a pyramidal structure. This is in two sense. First, viewing the distribution of population at different income levels, there is a clear pyramidal shape to that distribution: a large proportion of the population lies at the low end of the scale and a small proportion at the top. Associated with that pattern is another feature which conforms to an *inverted* pyramid, namely, a large proportion of the total income is appropriated by a small proportion of the population at the top and the bulk of the population at the bottom obtain a small proportion of total income. (One could plot all of this data, of course, in the usual form of a Lorenz curve. This would display a large bulge away from the 45 degree line, that bulge providing a measure of the skewness in the distribution of income.)

What one observes, therefore, in underdeveloped economies is a conspicuously high degree of skewness in the distribution of income. The picture varies significantly from one country to another. But it is a picture that is generally true of all underdeveloped economies. Moreover, this skewness is much greater for underdeveloped economies as a whole than for the advanced capitalist economies.

Furthermore, it is clear that the situation is getting worse over time and not better; there is a general tendency towards deterioration. Moreover, and this is even more striking, it does not appear to improve significantly with the growth performance of the economy. Thus, the common presumption – that growth would somehow take care of that problem by bringing new groups into the middle-income range thereby collapsing somewhat the skewness in the income distribution – does not seem to hold.

Another striking feature is that, outside of the socialist economies, it does not appear that this skewness varies very much with the extent of state participation in the economy. State participation may take the form of taxation, subsidies, and even state ownership; yet it does not appear to influence significantly the structure of income distribution. In Brazil and Mexico, for instance, there have been substantial growth in state intervention in this sense; nevertheless these countries continue to have a highly skewed distribution.

The other side of this picture, of course, is that the most dramatic shifts in the distribution of income have occurred in some of the socialist countries, Cuba, for instance. There seems to be, in their case, a genuine structural transformation that political transformation brings about.

What all of this evidence points to, I suggest, is a tendency towards concentration and polarisation of incomes associated with the process of economic development. At the very least, we might say that economic development tends to reproduce and sustain large differences in income between the top and bottom of the scale.

One may note that this holds both for differences within countries and across different countries in the world economy; they are two different aspects of a general phenomenon. The latter aspect I shall ignore for the purposes of this discussion, which will look more closely at the internal structure of income distribution.

What we have here is a problem which requires deep analysis because within the existing literature the kind of analysis usually offered is quite shallow and does not grapple with the deeper aspects of this problem.

Historical Origins

These tendencies have to be understood, in the first instance, historically. That is to say, it is a matter of the initial conditions which these countries inherited from a long process of historical development. In that respect, the conditions that we observe are not arbitrary; they are the outcome of a long-standing historical process which, for many countries, is associated with the period of colonial economy. As a result, these countries inherited a set of conditions that were produced within the colonial period, within a set of social and economic experiences that constitute colonial economy.

Specifically, the inherited conditions are the consequence of:

(1) the ownership relations created during the colonial period, which involved (as is well known) a high degree of concentration of property ownership, especially ownership of land;

(2) the production structure, which entailed utilisation of mostly unskilled labour performing menial tasks, as in the plantation system;

(3) the organization of distribution, involving the proliferation of middlemen between peasant producers and the market;

(4) monopoly relations in commerce and banking, yielding monopoly profits to a small class of people;

(5) deliberate policies of holding down wages, supported by the colonial state, which gave rise to the depressed incomes that one observes at the low end of the scale;

(6) reinforcement of these conditions by the apparatus of the state through

 (a) a regressive structure of income tax and excise duties;

 (b) failure to develop extensive systems of mass education and training so as to raise the skill level of the population;

(7) policies of racial and cultural segregation which tended to confine identifiable ethnic groups to specific kinds of occupations.

A point to note here which has some relevance to a country like Malaysia is that it is in this period that in some countries the pattern of income distribution comes to acquire a distinctly racial or ethnic character for a profoundly significant reason. Put simply, the reason is that the colonial system was a global system of reorganisation and reallocation of labor in which different ethnic groups were brought together on a global basis through the transfer, for instance, of labour from India and China and, of course, of Africans as slaves at an early date to the Caribbean and elsewhere. As a result certain ethnic or racial divisions were created by these tendencies which operated within the global colonial system. Correspondingly, what emerged in this period was an ethnic or racial structure of income distribution which was associated, in turn, with the specific position that different ethnic groups occupied in the social division of labor in the colonial economy, and with the timing of their entry into those positions. Thus we find, for instance, Africans and Indians performing menial labour on the plantation, Chinese as workers in mining and railway construction, Chinese and Parsi Indians as merchants and, at the top of this system, in the bureaucratic and administrative hierarchy as well as in ownership of the banking system and the plantations, the expatriates from the metropolitan centres of the colonial system. As such, there was a definite ethnic and racial character to the social structure which reveals itself in the pattern of income distribution. (The specific historical process of the development of social structure in Malaysia, as in any of the countries that fall into the scheme is, of course, a complex problem requiring much deeper analysis.)

But in general, I am suggesting here that the colonial economy consisted of a set of economic and social relations in which there were powerful *disequalising forces.* Those disequalising forces were the factors that tended to perpetuate and reproduce the social imbalances that show up in the skewed distribution of income.

The Modern Period

However, we have to distinguish between these conditions in the period of colonial economy and those to be found in 'the modern period'. In this latter period, we start off with an inherited set of conditions derived from the previous period of colonial economy. But, in addition, certain significant changes occur. These changes take place both on a political level, consisting of the achievement of political independence, and on a social level, for instance, the emergence of mass educational systems. They occur also on an economic level, in terms of rapid urbanisation, the beginning of industrialisation, and a process of movement out of the high degree of specialisation involved in one-crop economies into a more diversified pattern of production. What is striking, however, is that despite all these changes which have continued, the pattern of polarisation and concentration of income still persists and, in fact, takes new forms.

What we have here, therefore, is the existence of powerful mechanisms and forces, some of which are new and affect the process in a distinct way. What are these forces?

These forces, I wish to suggest, are associated fundamentally with the character of the process of capital accumulation. Specifically, they are associated with what is called the *uneven development of capital.*

Elements of this process are implicit in some of the discussions regarding the character of industrialisation. For example, it is commonly recognised that there exists a profound tendency towards economies of scale within the industrial sector. Interestingly enough, this tendency exists also within the agricultural sector. What this means is that there is a tendency for the larger units of production, whether farms or industrial firms, to have certain kinds of economic advantages enabling them to sell at lower costs than small units and, correspondingly, to erode their markets, hence achieving a dominant position vis-a-vis the smaller units of production. The other side of that coin is, of course, the growth of concentration and monopolisation within the production system.

Ultimately, this process results in the creation of a structural division within the economy. This structural division consists, on the one hand, of a sector of large firms operating under conditions of a market structure which may be highly monopolistic (in the case of industrial firms producing for the internal market), using highly advanced and sophisticated methods of production, and with an internal division of labor that forms a hierarchical structure of organisation and control within the firm. (Together with this hierarchical division of labor, there is a wide dispersion in incomes and wage rates within the firm; we see here, in fact, the economic force operating within industrial firms to reproduce and extend the skewness in the distribution of income.)

On the other side of this structural division, we find a proliferation of small firms, using highly labour-intensive methods of production and employing low-skilled and low-wage labour. The profits generated by these producing units are small by the standards of the larger firms so that, even within the category of profit income, there would be a corresponding skewness in the distribution.

What, however, are the underlying factors that give rise to the operation of economies of scale? Briefly, they are associated with a number of well-known conditions:

(1) the existence of indivisibilities in the production process, as indicated by the fact that it requires a large-scale plant in order to produce efficiently;

(2) the existence of economies in marketing, transportation and so on;

(3) the character of the process of technological change and the requirements of research and development.

But most important of all, I want to suggest, are factors operating through the financial system. These factors may well be decisive and are associated, firstly, with the conditions of internal finance of investment. In particular, the firms with higher profit rates can grow at a higher rate through the reinvestment of their own profits. Secondly, there is the factor of external finance associated with the policies of the banking and credit system. Larger firms clearly have better access to credit and hence are able to gain the financial leverage that enables them to grow more rapidly than smaller firms.

We therefore find a powerful tendency, aided and reinforced by the financial system, that generates the skewness in the production system in the structure of firms and, correspondingly, in the distribution of income.

All these factors, needless to say, operate within an international context in which international forces play a powerful role. The links that national firms have with international firms, for instance through 'joint ventures', tend to reinforce tendencies to concentration by strengthening the larger national firms vis-a-vis the smaller ones. Furthermore, the requirements of international competition on the part of national firms, especially those producing for export markets, dictate that they adopt a certain pattern of technology, a certain structure of organisation and control within the firm, and certain kinds of sales strategies which require employing large sales forces of highly-paid people. These are factors which derive from the fact of the economy being integrated within an international system in which firms must operate in order to secure their requirements of finance, technology and markets.

In addition to these powerful forces operating at the level of production and as between firms, there is the factor of persistent regional disparity which is in turn associated with what I call *conglomeration effects.* For instance, firms tend to locate where certain kinds of ancillary facilities and services are provided; this is usually in the larger urban areas. Hence, there is a tendency for urban incomes to polarise in relation to rural incomes. Urbanisation itself and demographic concentration in the cities contribute to a rapid growth of land rent and capital gains in urban real estate. These effects are reinforced and supplemented by the tendency of agricultural productivity to grow less rapidly than industrial productivity: with this persistent gap in productivity levels producing the huge gap between agricultural and industrial incomes.

The point that emerges from this analysis is that there are powerful forces operating in a cumulative way which, once started, feed on themselves, so to speak. These forces account for and generate the persistent pyramidal structure that we observe in the distribution of income.

The Role of State Action

The question that arises, then, is whether these forces can be checked or reversed in some significant way. If so, how and by whom? The standard answer is that the state must design policies that seek to redress the imbalances in the distribution of income. This is the inference that is usually drawn from the general picture of income distribution in underdeveloped economies. We have to examine, therefore, the potential for state action in altering the distribution of income.

To deal with this problem, it is usually suggested that the state can adopt a number of policies in particular:

(1) taxation, involving improvements in the progressive structure of the tax system;
(2) subsidies and income transfers;
(3) promotion of education;
(4) regional location schemes, involving provision of incentives to allow firms to relocate their production activity;
(5) a policy that seeks to counterbalance the role of monopoly forces in the economy by the creation of competitive influences.

The policies, it is argued, would redress the kind of imbalances we have seen. The question which this argument naturally raises is: how effective are those policies? The brief and straightforward answer, it seems to me, is that they have proved historically to have very limited effect. We need not go into the statistical grounds for this conclusion. It is important merely to point out here that there are reasons why this is so, and the fact that it is no accident that these policies have limited

effect. This is the point that has to be recognized in examining the statistical and historical record.

There are fundamental reasons why the state cannot redress these imbalances. In large part, it is due to the inherently contradictions of the situation. Specifically, in order to improve the distribution of income in favour of the low-income sector of the population it is necessary to pursue a deliberate policy of raising wages. But we know very well that raising wages implies reducing profits. There is, therefore, an obvious conflict involved at this level.

Another source of conflict is in the powerful role of international competition. As we have seen, it is no accident that national firms tend to adopt a certain pattern of technology and a certain structure of employment relations within the firm and to undergo a tendency towards concentration, hence widening and extending the gap in the distribution of income.

Ultimately, then, one might say it becomes a matter of 'political will', to use a term that has repeatedly cropped up. The problem, however, is that it is not clear what 'political will' means in view of the wide range of contexts in which that term is used. I mean by that that it is a question of examining the character of the state, a question which must be faced insofar as it is presumed that the state must redress these imbalances. For the fact is that there are obvious conflicts involved in seeking to alter systematically the distribution of income conflicts which set limits on the ability of the state of carry out such a programme. (The statistical record in fact suggests that the amount of the quantitative impact of state activities on these distributional conditions has been very small). This means, therefore, that there must be certain conditions in the character of the state itself and in the kinds of economic and political forces which lie behind the operation of the state that inhibit its ability to pursue sustained policies that would affect the distribution of income in a significant way. Thus, it is to the analysis of the political and economic basis of the state and the nature of the state in the modern period that, I submit, attention must be directed.